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AN ECONOMIC CRITIQUE OF SOCIALISM

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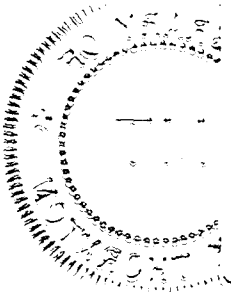

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The Journal of Libertarian Studies, Vol. V, No. 1 (Winter 1981)

Introduction

Collected together in this special issue of the *Journal of Libertarian Studies* is an apparently quite disparate group of articles on central economic planning, covering some theoretical disputes concerning it as well as some historical instances of attempts to put it into practice. These articles were written independently of one another, yet there runs throughout a single coherent theme: that the notion of planning an entire economy from the center is an utter sham both theoretically and practically. In practice, to the extent that economic production has ever been genuinely directed from a central economic agency, the results have been disastrous; and socialist economies have resorted to preserving only the guise of central planning for the ideological justification of Communist party rule. This catastrophic performance of central planning was lucidly explained theoretically by the Austrian economists Ludwig von Mises and Friedrich Hayek in the famous but tragically misunderstood "calculation debate." The lesson of these articles, then, is that central planning is an intellectually bankrupt approach to economic policy.

The central thesis of the "calculation argument" which underlies each of the contributions here is that "rational economic calculation"—which, under capitalism, takes the form of the accountant's calculation of profit and loss in terms of money prices—is impossible without private ownership of the means of production. Calculation of money profits and losses acts as a barometer of efficient performance without which economic production would be little more than stumbling about in the dark. Of the innumerable ways of combining resources that are *technologically* feasible, only a relatively tiny subset are also *economically* feasible. In order to get the most value out of the economy, some procedure has to be employed by which those economically more efficient production processes can be selected. And, since economic circumstances are never static, this procedure must be one that can operate continuously in the face of incessant change. The only such procedure that has ever worked is the calculation of profit and loss within a *de facto* private property system, and every step that economic policy has ever taken to supplant or obstruct this procedure in the name of "planning" has introduced an element of chaos rather than an element of deliberate control over economic life. Paradoxically, the more vigorous and consistent the attempt to consciously control an economy from the center, the more chaotic has been the result.

The essential point is that the order, the regularity, the *planfulness* of an

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economic system is a spontaneous resultant of the disorderly clash among the rivalrous plans of numerous competitors for profit. Through this very contention against one another are generated the institutions, especially the price system, by which economic production is rationalized. The price system, as Hayek puts it, acts as a telecommunications device through which the bits of specialized information that reside in decentralized form are summarized and dispersed in such a way as to tend to coordinate the various plans of the market participants. In this way a greater amount of knowledge is used by the economic system as a whole than can ever be mastered by any of the individuals who comprise this system. Prices act, in Mises' words, as "aids to the mind" which make possible an economic system of far greater complexity than could be designed by any individual mind. Thus did Mises argue in 1920 against the Marxists of the time who advocated the complete abolition of the price system.

But, it might be objected, everybody knows this now. Nobody anymore advocates *completely* centralized planning and the abolition of the price system. In both the East and the West we are treated to a policy of "market socialism" or "state-capitalist planning" in which the spontaneous forces of competition in the market place are guided, not replaced, by the rational goals of the central planning office to which, in the East, common ownership of the means of production is entrusted. The goal is no longer to replace but to monitor and manipulate the price system. Thus do contemporary socialists dismiss the arguments of Mises as obsolete against modern central planning theory.

However, this marriage of central planning with the decentralized price system is not so easily consummated. The Mises/Hayek argument contends that it is rivalrous competition among private owners which pushes prices in equilibrating directions and which thus imparts the relevant knowledge through prices to other decision-makers. The so-called "market socialists" in the calculation debate managed to evade this issue by rather disingenuously assuming at the outset that prices are all at their general equilibrium levels and then proceeding to demonstrate that, under this assumption, socialist managers could calculate just as easily as capitalist entrepreneurs. The market socialists neglected to offer any explanation as to how the Central Planning Board could miraculously hit upon this equilibrium set of prices, other than by random stabs in the dark described as the "trial and error" method.

Oskar Lange is generally thought to have successfully answered Mises' challenge by his elaborate "competitive" solution, according to which the results of a perfectly competitive equilibrium are to be simulated by handing down certain rules to plant managers to act *as if* they were private competitors. Thus, rather than being compelled to minimize costs by the struggle for profit, they will simply be *instructed* to price their product at the level where their marginal costs of production equal their selling price. In this way central planning proceeds by "playing at" competition.

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The elaborate market-socialist schemes that were invented in the thirties as supposed answers to Mises and Hayek have, significantly enough, never been put into practice. Rather than a central planning that "plays at" private competition, socialist economies, in practice, are more like competition that plays at central planning. Profit and loss accounting at the individual firm level, not some kind of Langean marginal-cost-equals-price rule, is in use in all socialist economies and has been ever since the brief attempts to eradicate it (twice in the Soviet Union, once in Cuba) proved so disastrous. All that the central planning apparatus accomplishes in the socialist economies—and, for that matter, all that economic interventionism accomplishes in state-capitalist economies—is to obstruct the coordination process of the price system, which manages to work in spite of the clumsy attempts to control it by government planning offices.

The essays that can fit into one issue of a journal cannot provide an exhaustive discussion of the many implications of the Misesian critique of central planning. At least as many questions will be raised as settled in these selections, but enough will be said here to constitute a substantive challenge to advocates of central planning.

The two selections by David Ramsay Steele which begin and end this collection are excerpted from an unpublished work called *The Impossibility of Communism*. Steele was an active Marxist in England for a number of years until he read, and was thoroughly convinced by, the arguments of Mises and Hayek. In this writer's opinion, his book offers the most conclusive critique of the Marxian vision of a future "post-capitalist" society that has ever been written. The portions that are presented here suffer somewhat from being removed from their proper context, and some arguments which appear here as mere assertions are more fully supported elsewhere in the book. However, many of these assertions will instead find adequate support in the essays by Robert Bradley, Sheldon Richman and myself.

In the opening selection Steele summarizes the meaning of the calculation argument as well as its early history, culminating in a clear challenge issued by Mises in 1920. Next, Bradley's essay offers a critique of Lange's "market-socialist" scheme, which the standard account of the debate claims had refuted Mises. The third essay, a chapter of a dissertation I completed recently under Prof. Kirzner, describes and criticizes this standard account of the debate, arguing that this account fundamentally misunderstood the challenge. Together these three essays argue that this challenge to central planning theory has been neither answered nor even understood by most of the economics profession, and thus deserves to be reconsidered.

The last two contributions go ahead to apply this Misesian challenge to a revisionist analysis of the history of central planning. Richman describes Lenin's initial, catastrophic attempt to plan the Soviet economy, which was finally and mercifully abandoned in the "New Economic Policy." Steele briefly takes up the NEP period and continues with an account of the

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second Soviet effort to abolish the price system—which was more quickly abandoned—and the similar attempt in Cuba. The remainder of Steele's essay examines the specific relevance of Soviet history to the Misesian challenge and concludes, contrary to the standard account, that it illustrates rather than refutes the calculation argument. The utter failure of the three genuine attempts at central planning, as well as the grossly inefficient but surviving systems of Stalinist-style pseudo-planning, are explained in the light of the Mises/Hayek argument.

While these contributions, like the Mises/Hayek challenge, focus primarily on the impossibility of genuinely planning a modern economy from a central bureau, they can be applied generally, with some modification, to more modest (and less consistent) schemes for piecemeal intervention into and regulation of a market society. While "interventionism" is clearly not impossible—since, as readers of this *Journal* are all too aware, it seems to be in practice everywhere—it can be shown to be self-defeating and irrational on much the same grounds on which Mises pronounced complete central planning impossible. The calculation argument reveals the spontaneous market order to be a discovery procedure by which knowledge of more efficient production processes is generated. That such knowledge cannot be entirely dispensed with explains the total collapse of every economy where central planning was completely substituted for the price system. But piecemeal government interference into the price system must, on this ground, be seen as similarly obstructive of this same, necessary discovery procedure, and therefore as distortive of the knowledge which it generates. Thus, the calculation argument may be used to explain many of the less-than-total failures resulting from government *tinkering* with the price system, in fundamentally the same way that it explains—as shown in these essays—the utter economic ruin inevitably resulting from attempted *abolition* of the price system.

The rhetorical appeal of the opponents of *laissez-faire* has always been that doing *something* must be better than, so to speak, sitting on one's invisible hands. Surely some producers must be reaping monopoly gains by selling at prices above their marginal costs of production in the unregulated market place, so the notion of conscious planning to correct the imperfections of unconscious competition seems like simple common sense.

However, even disregarding the tenuous ethical underpinnings of this argument, it can be maintained only by assuming that the economists at the central planning office can identify such quantities as marginal costs independent of the knowledge generated by the market process. They must be able to stand above the market and criticize its price information from a position of superior knowledge.

Granted this superior knowledge, the idea of *laissez-faire* is defeatist and unscientific dogmatism. However, the Misesian argument points out that we have no such store of knowledge, and that what we know about eco-

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nomic production we know only because we have relied on competition to tell us. Although competition does not miraculously yield—from the many possible outcomes—one *perfect* outcome, it does discover a *workable,* though admittedly imperfect, outcome, which we would have no way of finding without competition. The competitive price system is a procedure for discovering knowledge that we would otherwise lack.

If, as these essays contend, economists have no such knowledge, then the onus of proof shifts to those who contend that we should, even in our ignorance, modify the spontaneous market order. Being deliberately guided by conscious decisions rather than being "blindly" led by the impersonal forces of the market makes sense only if those who aspire to be our "guides" have better "eyesight" than that of the market. "Doing something" rather than "helplessly" leaving society to the forces of the "invisible hand" does not look so attractive once it is understood that the advocates of "doing something" are blind.

The calculation argument that is examined in the following essays shows that the profit and loss calculations of entrepreneurs are the "eyes" of the competitive system. The argument stressed here shows that this vision cannot be entirely dispensed with in the socialist program of planning; furthermore, the same argument extended shows that this vision cannot be improved upon by the manipulations of the unsighted interventionists in government.

Don Lavoie

The following essays on the socialist calculation debate have been collected and edited by Don Lavoie, George Mason University.

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Posing the Problem: The Impossibility of Economic Calculation under Socialism

by David Ramsay Steele

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The Economic Calculation Argument

For industry to be operated effectively, it is necessary that those in charge be able to perform "economic calculation." It does not matter at all, for the purposes of this argument, whether "those in charge" are professional managers, acquisitive capitalists, workers' councils or other democratically-elected assemblies, or holy men appointed by the gods. The problem of economic calculation which faces them is examined in more detail in some of the following essays, but the general idea can be explained very briefly and simply.

Those in charge of a productive unit, or enterprise (such as a factory), have to make decisions from time to time about how it will be run. They have to decide, for example, whether to instal a new kind of machine, or whether to switch from one technical process to another which will require different raw materials. Often they will have to select one plan out of dozens of possible alternatives. How are they to choose?

At first, the answer might seem obvious. They should choose "the best" or "most efficient." But that is not as simple as it sounds. It is not a task which can be performed unaided by those, such as scientists or technicians, who are familiar only with the physical operations involved. In fact, the major part of the problem is beyond the competence of technicians or scientists, and they are powerless to solve it for us.

As a simple example, suppose that we are in charge of an enterprise, and have to choose between two technical processes, A and B. Process A needs 50 tons of rubber, and 40 tons of timber, per week. Process B requires 40 tons of rubber, and 50 tons of timber, per week. The technical expert has informed us that A and B are both feasible alternatives for reaching a given end, but with that her work is done. Her purely technical knowledge does not enable her to go further, and tell us whether A or B is preferable.

If there were a third possible process, C, which used 35 tons of rubber and 35 tons of timber per week, to attain the same result as A or B, there would of course be no further problem: we would choose C. But between A and B we stand perplexed. Process A would enable us to save on timber, but

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at the expense of rubber. Process B would enable us to save on rubber, but at the expense of timber. Except for an improbable coincidence, one of them is the "better" method, the more "efficient," "productive" or "economical." The other is inefficient and wasteful. But which?

It is clear that we need some way of comparing timber and rubber, by reducing them to common units. It is equally clear that any and all *physical* units, such as weight or volume, would be irrelevant. (A gallon of water ought not to be equated with a gallon of mercury, nor a ton of sand with a ton of platinum.) We are perhaps tempted to say, rather hazily, that we want to be able to make a comparative valuation of rubber and timber in terms of their "scarcity," "costliness" or maybe "social importance."

In the market, such comparisons are made by referring to prices. The people in charge of the enterprise look at the market prices of rubber and timber, observing which is cheaper and which more expensive. If the price of rubber is $500 per ton, and the price of timber $1,000 per ton, then process A is cheaper than process B, and is more likely to be profitable.

The timber-and-rubber example is, of course, highly simplified. It would be more realistic to consider more than two processes, each of which utilized *numerous* factors, including various kinds of labor, with some of the inputs common to all the processes, though in different quantities, and some peculiar to one process only, or to a few of them. Then we would have to consider that the end results of the two (or more) processes might be different in detail, so that their comparative assessment might lead, say, to the conclusion that "the product of A is inferior to the product of B, but A is preferable nonetheless because of its considerably lower cost." We should remember that the vital role of economic calculation is by no means confined to major turning points in the life of the enterprise, such as the choice of a whole new technology, but extends also to the innumerable adjustments which have to be made every day, hour or minute. A production decision does not normally begin with all the "technical" facts, and only then proceed to the "economic" choice. Rather, the technician is aware from the outset of market prices, can therefore think in terms of "costly" and "cheap," and hardly ever makes purely technical calculations without the ever-present guidance of the market. Finally, prices change (and prices of factors of production generally change more frequently, unpredictably and substantially than prices of finished consumer goods). Therefore, the enterprise decision-maker does not merely read off the current prices, but tries to anticipate future prices, since the decision to adopt a specific course of action may have to be made well in advance of some of the resulting purchases of inputs. However, current and recent prices offer a very convenient starting-point for estimating future prices. All these qualifications show how much I have simplified the timber-and-rubber example in order to bring out clearly the essential point; but it will be

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evident that they do not *diminish* the importance of economic calculation using market prices, but on the contrary *increase* it.

I am not going to claim that reliance on market prices is a perfect method. At this point, suffice it to observe briskly that (a) market prices are spontaneous social products, resulting from an unplanned pattern of interactions among millions of people; (b) market prices generalize, encapsulate or sum up an immense amount of information which need not be, and generally is not, known to any single person or committee; (c) we can easily show that the influences which raise or lower prices, and thereby help to guide the behavior of those decision-makers who use these prices, are influences which would have to be taken into account, in broadly the same way, in any conceivable system for coordinating modern industry; (d) calculation using prices *works*, that is to say, prodigious industrial achievements have been brought to pass within societies which relied upon market prices.

As stated, I do not contend that market prices are *a perfect method* for performing economic calculation in an advanced industrial society. I contend that market prices are *the only method*. There simply is no other way. Therefore, market prices are essential to the survival of any complex industrial structure capable of generating high levels of material consumption.

The decisive demonstration of the impossibility of rational economic calculation under socialism was supplied by Ludwig von Mises in the spring of 1920, but Mises had his precursors. Hermann Heinrich Gossen, forgotten pioneer of marginal utility, had written as early as 1854:

> only through private property is the measure found for determining the quantity of each commodity which it would be best to produce under given conditions. Therefore, the central authority, proposed by the communists, for the distribution of the various tasks and their reward, would very soon find that it had taken on a job the solution of which far surpasses the abilities of individual men.[1]

Several nineteenth-century writers came close to a similar statement. Walter Bagehot pointed out that monetary accounting was indispensable in order to estimate costs of production, in any complex industrial society, and he coupled this with observations on the inability of primitive savages to perform calculations of profits or costs. He did not go on to draw the simple inference that developed industry without the market was an impossibility. Maybe he considered it too obvious to need stating.[2]

The Related Issues

Other writers directly tackled the question of a socialist economic order, but without isolating the calculation problem. Two lines of thought were

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pursued, which come very close to the economic calculation argument, but still leave it unformulated.

Wicksteed raised the issue of individuals' *remuneration* under socialism. From Wicksteed's discussion it seems almost certain that he had the economic calculation difficulty in mind:

> If public bodies were the only employers, on what principle should remuneration of the different agents be fixed? Is it possible to conceive of any machinery by which the marginal significance of each should be determined...?[3]

But he did not explicitly separate the question of allocation from the question of payment, because he was examining a hypothetical market socialism in which one enterprise after another was progressively taken over by the state.[4]

Other economists approached the socialist economy from a rather different angle. Without committing themselves on the ultimate feasibility of socialism, they pointed out that *if* a socialist society could and did come about, it would have to employ an allocative system closely parallel to that of the market. Socialism would have to "price" the factors of production, and would be compelled to use "rent," "interest" and "profit," or at least, bookkeeping notions strictly analogous to these. Such arguments were advanced by Wieser, Böhm-Bawerk (both 1889), Pareto (1897) and Barone (1908).[5]

The contributions of Pareto and Barone were to be curiously misrepresented later. Barone was a follower of Pareto, and they both expressed their ideas in mathematical equations based on those of Walras. The point of their arguments was to impress upon the socialists that any hypothetical socialist economy would conform to patterns similar to those found in a market. As far as I know, neither Pareto nor Barone gave a literal, categorical verdict on whether socialism was a practical possibility, though the very strong implication of their words is negative. What they did flatly state was that the function of the price system could never be replaced by the solving of equations. The equations only described the tendency of market prices; they could not be arrived at independently and used to replace market prices.[6] After Mises had raised the calculation issue, it was claimed that he had been refuted in advance by Barone, who had proposed that a socialist society could allocate its resources by the planners' sitting down and solving equations! Barone's blistering rebuttal of socialist misconceptions was hailed as if it had been a pioneering demonstration of the practicability of socialism. This bizarre story was given wide currency by Lange and Schumpeter, and has become part of the present largely fictitious consensus on the economic calculation debate.

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Pierson's Contribution

Following Kautsky's well-publicized speech in Delft, Holland, on *The Social Revolution*, the Dutch economist Nikolaas G. Pierson approached the question of the economic viability of socialism in a paper published that same year, 1902. Pierson's main concern is to emphasize that a socialist society would confront a "problem of value."

> The practical problem of value which is automatically solved [by the market]...would not disappear if its automatic solution were made impossible; it would remain in its entirety.[7]

After showing that a number of separate socialist states would have to regulate their mutual dealings with the aid of money prices, Pierson argues that a communist society would be unable to calculate "net income," since it would have no unit to perform the functions now performed by prices. The society would be unable to determine, say at the end of a year, whether it or any of its component parts had made a net gain or loss during that period. To draw up an inventory of all goods at two different points in time would not suffice: all these items would have to be expressed in common units of value.

Pierson examines the ways in which a socialist administration might ration out consumer goods, including the system of labor-vouchers, and shows that trading would re-emerge. He explains that

> the commercial principle, which such a society sought in vain to abolish, comes once more into the foreground....The phenomenon of value can no more be suppressed than the force of gravity. What is scarce and useful *has value*....to annihilate value is beyond the power of man.[8]

Dealing with Kautsky's suggestion that socialist "wages" could be fixed according to labor productivity, Pierson points out that this is not as easy as it sounds. Disentangling the contributions to output of all the different workers—determining the productivity of clerical workers compared with manual workers, for instance, let alone the contribution made by entrepreneurial awareness of fruitful possibilities—will be impossible without some assessment of economic "value." Pierson somewhat confuses the issue here by defending the "productivity" of advancing money. Presumably in Kautsky's socialism, though it retains money and wages, there would be no money loans to business enterprises. The entire question of which enterprises should be folded, which continued and which expanded would be determined by administrative means without the instrumentality of finance. Nevertheless, Pierson's point, that mere knowledge of opportunities can be immensely productive, stands.

All the essentials of the economic calculation argument are presented by Pierson.

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1. Society faces specifically economic problems, which cannot be reduced to the fields of competence of technologists or engineers.
2. These problems will not disappear under communism/socialism, but the present solution, the market (for factors of production), will disappear. Communism will have to find some alternative solution,
3. Any solution must take the form of comparing any and all goods according to common units denoting what Pierson calls their "value."
4. (By implication) Apart from market prices, no such units can be found. Therefore communism is impossible.

As Mises later acknowledged, "Pierson clearly and completely recognized the problem in 1902."[9] However, Pierson's approach is that of throwing out a number of suggestions about difficulties in operating a socialist economy. Apparently, he does not himself realize the relative importance of the points he is making. He overstresses international trade, in view of the fact that Marxists believe in world unification.[10] He often fails to separate the questions of allocation and remuneration, though he does clearly see that it "is possible...to carry out works at too high a cost, to put up buildings in the wrong places and to design them in a manner inappropriate to their purpose," and that this cannot be a purely technical matter, but must be one of "value."

Pierson's continual harping on the necessity of value may seem strange to a modern reader. But in 1902 any active socialist or critic of socialism would have known almost by heart the celebrated passage from *Anti-Dühring* in which Engels explained how very easy it would be to organize socialist production:

> Society can simply calculate how many hours of labour are contained in a steam-engine, a bushel of wheat of the last harvest, or a hundred square yards of cloth of a certain quality....society will not assign values to products. It will not express the simple fact that the hundred square yards of cloth have required for their production, say, a thousand hours of labour in the oblique and meaningless way, stating that they have the *value* of a thousand hours of labour. It is true that even then it will still be necessary for society to know how much labour each article of consumption requires for its production. It will have to arrange its plan of production in accordance with its means of production, which includes, in particular, its labour-power. The useful effects of the various articles of consumption, compared with one another and with the quantities of labour required for their production, will in the end determine the plan. People will be able to manage everything very simply, without the intervention of much-vaunted "value."[11]

Today, the myopia and economic illiteracy of this passage are painfully evident to anyone.

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Weber on Rational Calculation

It often turns out that a crucial breakthrough is made independently and almost simultaneously by several individuals. The economic calculation argument was separately given a full and clear statement in 1920 by Boris Brutzkus, Ludwig von Mises and Max Weber. Weber's version occurs in his *Economy and Society* which was not published until the following year.

Weber's treatment is slighter than those of Brutzkus or Mises, but in its context it is something of an aside, since the work is mainly an attempt to summarize the classification of "ideal types" which Weber believed necessary for the sociological study of modern Western economic and political institutions. This task, however, leads him to point out the limitations of "calculation in kind" by contrast with monetary calculation, an issue which was highly topical since in 1919 two influential socialist theorists, Otto Neurath and Otto Bauer, had each published books advocating a moneyless economy.[12] Weber refers specifically to Neurath, who argued that non-monetary calculation was already well established, that market prices were arbitrary anyway, since they did not measure anything, and that the German war economy had shown the way forward to a new "natural" (moneyless) economy.

Weber's argument is vitiated by his concern with an unsound (and not altogether intelligible) opposition between "formal rationality" and "substantive rationality."[13] He states that only the market can permit the achievement of a very high degree of formal rationality. His concept of substantive rationality is obscure, but it seems that Weber believes either that formal rationality is important in its own right, or else that it is a necessary condition of any substantive rationality. At any rate, he concludes that

> the possibility must be considered that the maintenance of a certain density of population within a given area is possible only on the basis of accurate calculation. In so far as this is true, a limit to the possible degree of socialization would be set by the necessity of maintaining a system of effective prices.[14]

This seems "substantive" enough. Weber acknowledges that non-monetary budgeting may be "rational" under very simple conditions, "so long as the situation does not require a very precise estimate of the comparative utility to be gained from the allocation of the available resources to each of a large number of very heterogeneous modes of use."[15] Non-monetary computation in small-scale, self-sufficient households, once it has to deal with factors of any complexity, is confined to "traditional standards" and "rough estimates," and cannot therefore cope very well with changing conditions.

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Rational accounting of any complexity requires money prices, and these require the autonomy of separate units. Fictitious prices, which do not correspond to those actually established by competing enterprises in a market, would be useless.[16] Calculation in kind may work to some extent where different ways of producing the same final good are being compared, or where a given supply of factors may be used in alternate ways to produce one of several kinds of goods.

> But the more difficult problems of calculation begin when it becomes a question of comparing different kinds of means of production, their different possible modes of use, and qualitatively different final products.... the comparison of different kinds of processes of production with the use of different kinds of raw materials and different ways of treating them, is carried out today by making a calculation of comparative profitability in terms of money costs. For accounting in kind, on the other hand, there are formidable problems involved here which are incapable of objective solution.[17]

A modern enterprise is perpetually confronted with the question whether each of its parts is paying its way, or whether any part is utilizing inputs that could more rationally be used elsewhere. This can be settled relatively easily and accurately using proceeds and costs expressed in money, but "it is exceedingly difficult to do this entirely in terms of material goods, and indeed it can be accomplished at all only in very simple cases." No technical improvements can save the day for moneyless calculation, asserts Weber: "really exact accounting" in kind is "impossible in principle." The main problem is one of imputation, attributing values to the factors of production. Any non-monetary system of accounting would have to set up "indices of the value" of different resources which would have to play a role similar to that of market prices. But there is no way of establishing such indices:

> Nothing is gained by assuming that, if only the problem of non-monetary economy were seriously enough attacked, a suitable accounting method would be discovered or invented. The problem is fundamental to any kind of complete socialization. We cannot speak of any kind of a "rational planned economy" so long as at this decisive point we have no way of working out a rational plan.[18]

Brutzkus and Bolshevism

Boris Brutzkus was an economist caught up in the Russian revolution, the subsequent Bolshevik takeover, and the attempt by the Bolsheviks to usher in a communist order. In August 1920 the Bolsheviks were at their hour of greatest glory. They had defeated the "counter-revolutionary" forces in the field, and fastened their own unchallenged rule onto the Russian Empire. The abolition of money was in progress: the communist economy was

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visibly taking shape. Its impoverishing dislocations of production could still be blamed on the recent wars. At this moment, Brutzkus delivered a lecture to an academic audience in Petrograd, explaining that "the system of Marxian communism, as then conceived, was—quite apart from the conditions produced by the war—intrinsically unsound and must inevitably break down."

Seven months later, the Bolsheviks found themselves compelled, if they wished to remain in power, to abandon the pursuit of communism and deliberately foster the market economy. At the same time, there was a temporary relaxation of political repression. Some criticisms of the regime were permitted to appear, subject to a rather mild censorship. Brutzkus published the substance of his lecture in a learned journal, and only a few paragraphs were deleted by the state. In the summer of 1922, political repression was intensified once more. Many anti-Bolshevik academics were rounded up and ordered to leave the country. Trotsky described this policy as "preventive humanity," and argued that

> Learned ideologists are not at present dangerous to the Republic, but external or internal complications might arise which would oblige us to have these ideologists shot. Better let them go abroad therefore.[19]

Trotsky probably did not dream that the same preventive humanity would before long be accorded to him.

In the 1921 articles based on his 1920 lecture, Brutzkus points out that "scientific socialism" has confined itself to criticizing the capitalist order, without paying any serious attention to the organization of socialist society. Both the Western social democrats and the Russian Bolsheviks found themselves in power without possessing the comprehensive plan which would obviously be required for the construction of socialism. Nonetheless, the outlines of Marxian socialism are clear: it is on a large industrial scale, and it replaces the "anarchy of production" with a unitary plan. There are therefore no wages, profits, rent or other prices.

Brutzkus argues that any economic activity "must obey the principle that its results must correspond to the costs expended upon them."[20] In a primitive, small-scale society this is fairly easy. In the "capitalist system" the principle is obeyed by making sure that goods can be sold at a price which covers their costs of production. "This evaluation takes place by virtue of a spontaneous process, the results of which must be taken by the entrepreneur as data." But when central planning has supplanted the market, these data will clearly not be available.

After dismissing the suggestions of Bukharin and Tschayanoff that calculation in kind could be performed, Brutzkus considers the idea of using "labor" as a measure of production costs. There is no way of reducing all the varying qualities of labor to a single homogeneous measure, and "labor value" would fail to take account of the current scarcity of capital

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goods. Furthermore, it is only in a hypothetical and never-to-be-reached equilibrium that market prices would equal past production costs (and hence, if we assume that all production costs can be reduced to labor, to "labor values"). The actual divergencies of market prices from costs of production represent important influences which ought to be taken into account, and which would therefore have to be included in any method proposed to replace market prices.

The socialist planners would have to quantify everyone's needs, and then specify the means of attaining them. Brutzkus believes that even to measure the population's requirements for foodstuffs would be extremely difficult, and to estimate all their needs would be beyond the capabilities of any administrative body.[21] But this is not the main problem. In the market, enterprises must pay their way or close down; but under socialism, "there exists no direct connection between the productivity of an undertaking and the supply of funds for its continuance." Nor could there be any such connection, for

> under socialism there is no general measure of value. Suppose that a Soviet estate has contributed so and so much milk, so and so many pounds of meat, so and so many bushels of grain. How many pounds of best quality seed, how much artificial manure or oil cake, how many head of breeding cattle or suits of clothes and how much fuel may the estate claim in return for its products?...in a society without markets the problem is insoluble.[22]

Brutzkus presents a number of other arguments not central to the economic calculation question. He points out that if the socialist authorities once accept the need to keep material rewards for work in proportion to the productiveness of the work, they will be bound to introduce rent, interest and profit. He argues that there are no grounds to expect any enhancement of personal freedom, much less the abolition of the state, from any attempt at socialist planning, and calls into question the view that people will work more enthusiastically in a socialist society. Finally, he claims that conditions in Russia, with its self-sufficient isolation and highly concentrated industry, have been rather favorable to the institution of socialism. Consequently, its failure there is an especially conclusive refutation.

The Classic Statement

Of the trio which unleashed the economic calculation argument, Weber, Brutzkus and Mises, the outstanding figure was undoubtedly Mises.[23] His statement was published first, it was soon incorporated into a comprehensive critique of socialism in all its aspects, *Die Gemeinwirtschaft (Socialism: An Economic and Sociological Analysis)*, it quickly reached a wide audience of socialists and was so stinging and provocative that it could not be ignored. Judged from the viewpoint of exposing the weakness of

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socialism as a practical project (which was not Weber's primary purpose), Mises' contribution was much more pertinent and detailed than Weber's, and also more exact and succinct than Brutzkus'. The socialist economist Oskar Lange, in a sarcastic observation with serious overtones, stated that Mises' services to socialist theory were such that a statue of him ought to occupy an honorable place in the great hall of the socialist society's Central Planning Board. True, the statue has not so far materialized. But then, neither has any Central Planning Board of the kind envisaged by Lange.

In his "Economic Calculation in the Socialist Commonwealth," Mises emphasizes that the way in which consumer goods are distributed is a secondary matter. Like Pierson before him, he points out that once individuals in a socialist society have collected their "coupons," trade will emerge. But this trade will be confined to consumption-goods. Production-goods, because they will be owned by "the community," cannot be subject to commercial transactions.

> Just because no production-good will ever become the object of exchange, it will be impossible to determine its monetary value. Money could never fill in a socialist state the role it fills in a competitive society in determining the value of production-goods. Calculation in terms of money will here be impossible.[24]

Under simple conditions, a Robinson Crusoe, or a family of subsistence farmers, would not only value consumption-goods, but would also be able to impute value to production-goods. If fish were valued, so would be a fishing net. If wild boar were valued, so would be a spear. Even at such a simple level, the producers would have to take account of "the intersubstitutability of goods." Some production-goods could be used for producing alternative consumption-goods in different quantities. Crusoe would have to make a rough-and-ready estimate of the importance of these production-goods, but he would not, of course, be able to total costs of production in money prices. Neither would he have access to any units which could enable him to assess whether a contemplated course of action (such as building a highly elaborate boar trap with materials which could be used for other purposes) was worth it.

In a society with a more complex technology, the rough-and-ready estimates employed by tiny bands of hunters and farmers would be useless. Here, assessment is made in terms of costly or less costly, dear or cheap, as demonstrated by objective exchange-value: market prices expressed in money. The use of objective exchange-values for economic calculation "entails a threefold advantage." Calculation can be based upon the valuations of all participants in trade; there is in monetary profitability an immediate and sure indication of economical production; and values can be referred to a common unit.

Two conditions are necessary before monetary calculation can be

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employed in directing production. First, higher-order goods (capital goods) must be exchanged, as well as first-order goods (consumption-goods). It is not enough to be able to value first-order goods, because

> No single man can ever master all the possibilities of production, innumerable as they are, as to be in a position to make straightway evident judgements of value without the aid of some system of computation. The distribution among a number of individuals of administrative control over economic goods in a community of men who take part in the labour of producing them, and who are economically interested in them, entails a kind of intellectual division of labour, which would not be possible without some system of calculating production and without economy.[25]

Second, there must be "a universally employed medium of exchange," money, used in the exchange of means of production as well as consumption-goods. Otherwise it would be impossible to reduce all the many exchange-relationships to a common denominator.

It is no use appealing to existing examples of state-directed concerns, for these are islands of "socialism" within the market, having access to market data. Nor can socialism merely continue what was done previously within the market, for with changing conditions, the old methods of production will "become irrational."

Because the socialist planners will be unable to reduce all the means of production to a common denominator, they will be confined to hazarding "vague estimates." The possibility of exact calculation disappears with the price system. "Where there is no free market, there is no pricing mechanism; without a pricing mechanism, there is no economic calculation."[26]

As a possible way out, Mises considers the division of industry into branches controlled by "syndicates" permitted to trade with each other. However, no useful prices could emerge except where the syndicates' autonomy was such that they held *de facto* property rights in their means of production:

> This would not be socialization but workers' capitalism and syndicalism.[27]

Today we might call this "market socialism," a term that would have sounded very strange in 1920. Mises makes it clear that he regards "workers' capitalism and syndicalism," in this context, as a form of "private ownership of the means of production." It is effective control by sections of society, instead of unitary control of all resources from a single center.

Mises dismisses on two grounds the suggestion that labor-hours could be used to estimate production costs. It ignores the different qualities of labor, and it does not take into account unproduced natural resources. The latter point applies even if, along the lines of the Marxian theory of value, we

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subsume under "socially necessary labor-time" all natural resources as and how they are used up in production:

> Let the amount of socially necessary labour-time required for the production of each of the commodities *P* and *Q* be 10 hours. Further, in addition to labour the production of both *P* and *Q* requires the raw material *a*, a unit of which is produced by an hour's socially necessary labour; 2 units of *a* and 8 hours' labour are used in the production of *P*, and one unit of *a* and 9 hours' labour in the production of *Q*. In terms of labour *P* and *Q* are equivalent, but in value terms *P* is more valuable than *Q*. The former is false, and only the latter corresponds to the nature and purpose of calculation.[28]

Mises also advances the argument that people cannot be expected to display suitable initiative in an organization in which they have no personal stake, but he observes that even if this objection were of no account, the economic calculation argument would be decisive. After a brief review of the inconclusive remarks of Otto Bauer and Lenin on the running of a socialist economy, Mises finishes by declaring that although "rational economic activity is impossible in a socialist commonwealth," this need not deter those socialists motivated by ascetic ideals, nor those prepared to abandon material affluence for the sake of the ethical goal. Mises does not dispute that "socialism" is possible at a low level of technology and consumption.

What Mises Meant by "Socialism"

Mises always made clear what he meant by socialism, a society without private ownership and market exchange of the means of production. Socialism might or might not do away with money altogether, but it would by definition do away with monetary exchange of factors of production. In socialism, social production would be planned and managed as a single unit by a single supreme planning body.

There is no question but that this conception of socialism corresponded to that of the vast majority of avowed socialists in 1920, and for some time afterwards. One indication of this is that Brutzkus and Weber independently took it for granted, and the earliest respondents to Mises did not challenge it. However, Mises did exaggerate slightly in claiming that "all socialists before 1920" held that "socialism necessarily requires the abolition of the market and of market exchange and even that this fact is both the essential element and the preeminent feature of a socialist economy."[29] To make this statement correct, it is necessary to put "Marxist socialists" instead of "socialists," and "market for industrial means of production" instead of merely "market." As a matter of fact, the earliest socialists, the followers of Saint-Simon, did not commit themselves to the total

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elimination of the market, and Proudhon was an early "market socialist." The *Communist Manifesto* execrated "bourgeois socialism," which sought to reform instead of abolish "the bourgeois relations of production" (private property and the market). It was the growth of Marxism at the expense of other socialist schools which led by the turn of the century to the predominance of the strictly non-market idea of socialism and which was almost taken for granted in the German-speaking world when Mises penned his critique.

It may clarify matters to distinguish four varieties of projected socialism.

1. Marxian communism. Total abolition of the market, money and prices. Distribution of consumer-goods either by ration tickets, such as labor-vouchers (definitely *not* money) or by free access. Coordination of production to be achieved by central planning, using technical data only, not prices.
2. What we might loosely call "Communist production, market distribution." A market exists for consumer goods only. Either it emerges spontaneously on the basis of the ration tickets mentioned above; or the planning authority deliberately allows for such a market, pays everyone in tickets which can be transferred and accumulated, and somehow prices consumer goods so that they can be acquired from "the community" (i.e., the planning body) in exchange for the tickets. All production goods are owned by "society"; therefore they do not change hands on a market, and have no market prices.
3. Proposed systems which, while not explicitly either of the above, contain features which must lead to one of the above. (For example, if it were proposed that all prices should be fixed centrally by the state, this would mean that the state would have to determine all physical quantities and technical processes, too. The "prices" would cease to be real prices at all, and the market for factors of production would be ruled out.)
4. Out-and-out "market socialism," in which there is a market for both consumer goods and means of production.

According to Mises, the first three are practically impossible, in conjunction with large-scale industry and division of labor. The fourth is entirely feasible, though it amounts to acceptance of everything which most socialists for the past hundred years have been denouncing as capitalism. It is possible that market socialists may reject some of the institutional requirements and social consequences of a market for factors of production, in which case their position is internally inconsistent. For example, a society with a market for factors of production is one where industry is governed by "the profit motive," and where neither incomes nor wealth holdings can be equalized.

Mises defined socialism in terms of ownership by "the community." In passing he indicated that this could mean nothing other than state ownership, but he did not wish to be sidetracked by a merely semantic argument.[30] Although the rhetoric of modern socialism has generally been democratic, appealing to the interests of the masses, the economic calculation argument applies to *any* centrally-directed system:

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> A socialist community can have only one ultimate organ of control.... It does not matter whether this organ is an absolute prince or an assembly of all citizens organized as a direct or indirect democracy. It does not matter how this organ conceives its will and expresses it. For our purpose we must consider this as accomplished.[31]

As Rothbard has pointed out,[32] the argument applies equally to the notion of "One Big Firm," a single cartel or trust emerging from the market. Such a firm would be unable to calculate and would swiftly disintegrate. In practice, this means that the free market places a limit on the extent of even partial monopolies. The growth of such monopolies must lead to the indeterminacy of prices, with consequent losses and the re-assertion of competition.

NOTES

1. Quoted in Ludwig von Mises, *Socialism: An Economic and Sociological Analysis* (London: Jonathan Cape, 1951), p. 135.
2. Bagehot, *Economic Studies* (London: Longmans Green, 1898; reprint ed., Clifton, N. J.: Kelley, 1973), pp. 54–58.
3. P. H. Wicksteed, *The Common Sense of Political Economy* (London: George Routledge and Sons, 1933), 2:682.
4. Actually there can be no possibility of separating allocation from remuneration, but this is a conclusion drawn *from* the economic calculation argument, and to state the argument clearly it is necessary, as a preliminary, to separate the two issues.
5. Friedrich von Wieser, *Natural Value* (London: Macmillan, 1893), passim; Böhm-Bawerk (on the need for interest under socialism), *Capital and Interest* (South Holland, Ill.: Libertarian Press, 1959), 2:341–46; Vilfredo Pareto, quoted in F. A. Hayek, *Individualism and Economic Order* (London: Routledge and Kegan Paul; Chicago: University of Chicago Press, 1949), p. 140; Enrico Barone, "The Ministry of Production in the Collectivist State," in Hayek, ed., *Collectivist Economic Planning* (London: George Routledge and Sons, 1935).
6. This point is pursued in the following chapter of the work from which this paper has been excerpted.
7. Nikolaas Pierson, "The Problem of Value in the Socialist Community," in Hayek, *Collectivist Economic Planning*, pp. 60–61.
8. *Ibid.*, p. 75.
9. Mises, *Socialism*, p. 135.
10. Few participants in the economic calculation discussion have paid any attention to the fact that Marxist socialism demands central planning *on a worldwide scale.*
11. Friedrich Engels, *Anti-Dühring: Herr Eugen Dühring's Revolution in Science* (Moscow: Foreign Languages Publishing House, 1962), pp. 424–25.
12. Otto Neurath, *Durch die Kriegswirtschaft zur Naturalwirtschaft* [Through the War Economy to the Natural Economy]; Otto Bauer, *Der Weg zum Sozialismus* [The Road to Socialism]. Neurath's work is now available in English as "Through War Economy to Economy in Kind," in a collection of his writings: Marie Neurath and Robert S. Cohen, eds., *Empiricism and Sociology* (Dordrecht, Holland: D. Reidel, 1973). His argument is briefly dealt with in T. J. B. Hoff, *Economic Calculation in the Socialist Society* (London: William Hodge, 1949), pp. 48–51.
13. Max Weber, *The Theory of Social and Economic Organization* (New York: Free Press of Glencoe, 1964), pp. 184–85.
14. *Ibid.*, p. 207.
15. *Ibid.*, p. 188.

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16. *Ibid.*, p. 194.
17. *Ibid.*, pp. 203–204.
18. *Ibid.*, p. 205.
19. Quoted in Boris Brutzkus, *Economic Planning in Soviet Russia* (London: George Routledge and Sons, 1935), p. xvii.
20. *Ibid.*, p. 9. Part 1 of this book consists of Brutzkus' 1921 articles.
21. *Ibid.*, p. 44.
22. *Ibid.*, pp. 45–46.
23. Mises, "Die Wirtschaftsrechnung im sozialistischen Gemeinwesen," *Archiv für Sozialwissenschaft und Sozialpolitik* 47, no. 1 (April 1920). Translated as "Economic Calculation in the Socialist Commonwealth," in Hayek, *Collectivist Economic Planning*.
24. Mises, "Economic Calculation," p. 92.
25. *Ibid.*, p. 102.
26. *Ibid.*, p. 111.
27. *Ibid.*, p. 112.
28. *Ibid.*, p. 113. If we follow Marx's usage, there would be *no* "value" under socialism/communism and hence no application of the labor theory of value. There is no evidence that Marx intended his labor theory of value to have any bearing on the organization of socialist production; it is a theory to account for relative prices under capitalism. Mises writes of "the labor theory of value" as a basis for socialist calculation, but if we read this as "accounting in socially necessary labor-hours," the argument is not affected.
29. Mises, *Human Action: A Treatise on Economics* (Chicago: Henry Regnery, 1963), p. 707.
30. Mises, *Socialism*, p. 129.
31. *Ibid.*, p. 130.
32. Murray N. Rothbard, "Ludwig von Mises and Economic Calculation under Socialism," in Laurence S. Moss, ed., *The Economics of Ludwig von Mises: Towards a Critical Reappraisal* (Kansas City: Sheed and Ward, 1976), pp. 75–76.

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Market Socialism: A Subjectivist Evaluation

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This essay is an attempt to provide a modern overview of the economic calculation debate from the Austrian School perspective. Specifically, the many arguments against market socialism will be consolidated to demonstrate the neglected theoretical strength of the free-market perspective. In this regard, the fact that market socialism never has been implemented or even become a ballot box alternative can be better understood.

The seeds of the calculation debate had been planted by a host of economists before Ludwig von Mises posed the central question "in such a form as to make it impossible that it should ever again disappear."[1] Mises' article, adapted from a lecture of a year earlier, appeared in the spring of 1920 entitled "Economic Calculation in the Socialist Commonwealth."

The famous challenge of Mises was uncompromising and to the point: "Where there is no free market, there is no pricing mechanism: without a pricing mechanism, there is no economic calculation."[2] Two years later the argument was enlarged in a wide-ranging critique of socialism, entitled *Die Gemeinwirtschaft*, after which replies from his critics began.[3] Mises defended his position in articles published in 1924 and 1928 against, in Hayek's estimation, "objections [that] were really more quibbling about words caused by the fact that Mises had occasionally used the somewhat loose statement that socialism [economic calculation] was impossible."[4]

The main effect of Mises' arguments has been best summed up by the renowned socialist economist Oskar Lange: "It was [Mises'] powerful challenge that forced the socialists to recognize the importance of an adequate system of economic accounting in a socialist economy. Even more, it was chiefly due to Professor Mises' challenge that many socialists became aware of the very existence of such a problem."[5] But the real effect, looking on the challenge from a later date than Lange, was to force the socialists to retreat from a pure advocacy of Marxian socialism to a compromise watered down with "competitive" infusions—market socialism. It is this latter system, especially as developed by Lange, Lerner and Taylor, that will be examined below.

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Part I: The Foundations of Market Socialism

The heritage of the market socialists lies not as much in the Marxian tradition as in the early work in neoclassical equilibrium theory.[6] In particular, Leon Walras[7] pioneeringly proved the existence of equilibrium in all markets by the mental construct of having an auctioneer call prices until the supplies and demands of all markets meshed. The significance of this theoretical proof for the socialists was not so much that potentially a perfect order could arise from complexity, but that this order deliberately was engineered, so to speak, from the center.

Vilfredo Pareto, Walras' student and heir at the Lausanne school, then added an important condition by putting forward a verbal law of optimality in such an interconnected general equilibrium for both consumers and producers.[8] From Pareto's demonstration came the welfare ideal of "pure and perfect competition," which later was to serve as the optimality model for the market socialists to try to duplicate.

The next major contribution that proved (in retrospect) significant for the market socialists came from the pen of Enrico Barone. He conceptually solved the problems of production via mathematical equations. So, assuming one had sufficient information, the equations could be filled in and production optimally directed.[9]

Together, the above members of the early neoclassical group, in addition to giving their own school identity, laid the necessary groundwork for a separate school to follow.[10]

Part II: The Rules of Market Socialism

The elaborate plan for market socialism to achieve economic calculation has been provided by Oskar Lange in his essay "On the Economic Theory of Socialism." Lange begins by tracing the neoclassical theory of capitalism and its program describing optimality. This excursion provides Lange with a model needing duplication (and in parts improvement) within the constraint of state ownership of the means of production.

The "market socialism" model begins by assuming that the consumers exercise freedom in consumption. They are "sovereign," as under capitalism, providing the "guiding criteria" for the production processes.[11] Similarly, as laborers, they are free to choose the occupation "paying the highest wages."[12] The caveat exists, however, that the Central Planning Board (CPB) makes sure that "the distribution of the social dividend... be such as not to interfere with the optimum distribution of labor services between the different industries and occupations."[13] Further, this optimum requires that "the social dividend be distributed so as to have no influence whatever on the choice of occupation."[14] Thus, Lange's occupational freedom is preserved within the spirit of socialist egalitarianism.

The controversy surrounding socialism does not so much concern the

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above; rather, it concerns production and how socialism can have accurate factor pricing without competition. Lange here introduces several rules that are intended to replace and improve upon capitalist production. The first rule is to have all producers equalize the ratios of marginal productivity to their prices, for all the factors of production (e.g., $\frac{MP_a}{P_a} = \frac{MP_b}{P_b} = \frac{MP_n}{P_n}$).[15]

The second rule, to be used in tandem with the above, is to price production equal to marginal cost, a principle first recommended by Fred Taylor and readily adopted by Lange.[16] This marginal cost principle, the welfare ideal of neoclassical economics, is addressed not only to the singular firms but to the industries as well.[17]

The above two rules regulating socialism's capital structure can be viewed profitably alongside their free-market counterparts. Profit maximization under capitalism is replaced by producing at minimum average cost.[18] Free entry/exit and the optimum size of plant in the market order are likewise duplicated by the same rule.[19] The second rule, of setting price to marginal cost, conforms to the "pure and perfect competition" ideal under capitalism. Setting marginal benefits to marginal costs is seen as maximizing welfare (the Pareto optimality) for society. In all, the rules fully cover the economics of production, "determin[ing] the combination of factors of production and the scale of output" while also maximizing welfare.[20]

There remains one key procedure in the socialist plan, for pricing at marginal cost and production at minimum average cost assume that the prices reflect scarcity values. Again drawing upon the procedure formulated by Professor Taylor,[21] Lange instructs the CPB to set prices in response to shortages and surpluses in inventory levels. If there is a shortage, an adjustment in price upwards is necessary; if there is a surplus, the price needs lowering. Lange sees this method as effective and not unique since this is "the same process of trial and error by which prices on a competitive market are determined."[22] So, starting with historical prices and making "small adjustments" in response to inventory signals, true scarcity prices are found, since demand is entered to meet supply.[23]

Lange is careful to avoid rationing instead of adjusting prices since this interferes with prices being *parametric*.[24] The only exception would be when "there is general agreement that such deviation is in the interest of social welfare."[25]

With the carrot of profit replaced, the stick of the CPB becomes the enforcer. If the rules are not being followed, the CPB will "interfere" and "order" changes so that the prescribed harmony in production resumes.[26] "Fixing quotas of output and comparing them with the actual achievement" is one such check, offers Lange.[27]

Outside the area of prices for consumer and producer goods, there remains the all-important "price" of interest. In the short run, Lange en-

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visions the forces of supply and demand as spontaneously finding an equilibrium rate. But in the long run, the CPB would "evaluate the optimum time-shape of the income stream."[28] This is a key function, notes Lange, since the rate of growth in the socialist community is controlled.[29]

Professor Lange has been joined by Abba Lerner in theorizing about the conditions of efficiency under market socialism. Reflecting his familiarity with Austrian marginalism,[30] Lerner proposes to replace Lange's statics with dynamics, recommending that the rule of marginal *opportunity* cost be employed.[31] However, because his "marginal opportunity cost" is an equilibrium concept, Lerner's model is also essentially static. Thus little revision has been made regarding Lange's proposals.

There is no hesitancy on Lange's part in claiming that he has successfully rebutted the challenge of Mises, and though he treated the restatements by Hayek and Robbins as a more plausible "second line of defense," he was to conclude later that, "In my essay ['On the Economic Theory of Socialism'] I refuted the Hayek-Robbins argument by showing how a market mechanism could be established in a socialist economy...by...trial and error."[32] But Lange is not alone in his conclusion. As Don Lavoie points out in the accompanying essay, a number of eminent economists have reached a similar verdict that constitutes an unchallenged orthodoxy in the Comparative Economics field.

Part III: Competition: Austrian Versus Neoclassical Theory

After the socialists had refined their arguments in response to the Mises demonstration of the inadequacies of the Marxian system, several critical examinations of the new position were made. In 1940, Hayek published an essay entitled "The Competitive 'Solution'," which was the last of three major articles by him contributing to the debate. Mises also examined the Lerner-Lange-Taylor revisions with systematic rigor in his treatise of 1949, *Human Action*, under the title "Recent Suggestions for Socialist Economic Calculation." This was Mises' last reply.[33]

To appreciate the "Austrian" objections against the market socialist theory, one must take an important detour into a critical examination of neoclassical theory. This is of utmost importance since the Mises-Hayek insights have been wedged, by a great many students of the debate, onto the alien foundations of neoclassical equilibrium theory. Regarding this, it must be clearly pointed out from the start that the two schools have very different perspectives in judging and understanding competition and optimality. Specifically, the neoclassicists' emphasis on *equilibrium* is to a degree similar to the Austrians' emphasis on the equilibrating *process*. Since the two are nonoverlapping, this distinction should be kept always in mind.

The market socialists, as before mentioned, borrowed from the "pure and perfect competition" model the condition that prices be set at marginal

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cost. Furthermore, that real-world capitalism deviates from the above Paretian optimality is mentioned as a point against the allocation of resources under capitalism.[34]

A complete dismissal of the above and a contrasting view of competition couched in dynamic terms has been made by Hayek in a neglected 1946 essay, "The Meaning of Competition." Opening his censure, he states:

> [What] the theory of perfect competition discusses has little claim to be called "competition" at all. . . . The reason for this seems to me to be that this theory throughout assumes that state of affairs already to exist which, according to the true view of the older theory, the process of competition tends to bring about (or to approximate) and that, if the state of affairs assumed by the theory of perfect competition ever existed, it would not only deprive of their scope all activities which the verb "to compete" describes but would make them virtually impossible.[35]

What Hayek wants, instead of the static ideal, is the study of disequilibrium movements from one situation to another, while asking ourselves two questions: first, is the change coordinating (equilibrating) or not (disequilibrating)?; and second, what is the nature of these forces?[36]

To Hayek, then, "competition is by its nature a dynamic process whose essential characteristics are assumed away by the assumptions underlying static [perfect competition] analysis."[37] He asks: Can we call something competitive that does not allow for advertising, price undercutting, product differentiation, locational advantages, goodwill, imperfect (costly) knowledge, and the *new*?[38]

We now can see what competition means from the Austrian point of view. Rather than achieving a "perfection" that could never be realized, competition represents a framework of free entry and exit of firms (Machlup's "pliopoly") in response to uninhibited entrepreneurial foresight. As Israel Kirzner states: "Competition, in the process sense, is at least potentially present so long as there exist no arbitrary impediments to entry. . . . The competitive process depends entirely on the freedom of those with better ideas or with greater willingness to serve the market to offer better opportunities."[39] This distinct view of competition, in order to differentiate it from the "pure and perfect competition" model, may be labeled "rivalrous competition."[40]

One may examine the neoclassical (and market socialist) view of ideal competition from another perspective by asking the question: What would the world be like under a blanket of "pure and perfect competition"? First of all, as Hayek first noticed, there would not be an economic problem. For, given the assumption of perfect knowledge, complete efficiency is assumed. Scarcity may not be eliminated, but the best alternatives to deal with it are in employment.[41] Thus, there remains nothing for the actors to do to improve their condition—purposiveness has become obsolete. Further,

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the model is marred by logical quagmires. For example, an infinite supply cannot alter price or scarcity. And with perfect knowledge, the demand for cash balances would fall to zero, making prices soar upward toward infinity.[42] This, of course, is incompatible with the assumption of constant money prices under the model.

Logical inconsistency is not the only drawback to the idea of "pure and perfect competition." One can also question the model as a social optimum. One problem is its disregard of cost economies, resulting from factor indivisibilities, that exist under "imperfect" competition. Prices may be set at marginal costs and equal to average costs, yet be higher than necessary. In this context, the economist must remind himself that, dynamically, profits are not so much added to costs as created out of costs. So in all, we can envision a "perfect competition" price as being *higher* than an "imperfect" competition price. Also, "perfect competition," being set in a world of *givens*, cannot offer improved or new items. Furthermore, any and all consumer desire for diversification must be ignored as having a utility less than the "lower" cost of product homogeneity.

In contrast, the interesting problems (and *the* problem of economics) are to be found in the real world of incomplete information, shifting expectations, changing opportunities, error, and plan adjustment—*disequilibrium*. And, as Hayek notes, it is here that economics becomes an empirical science rather than a science of pure tautology.[43]

Part IV: Socialism and the "Trial and Error" Proposal

The above excursion should shed much light on the source of the Austrian criticisms. In Mises' original article and throughout the exchange, there have been explicit efforts by the Austrians to shift the plane of discussion away from equilibrium. In fact, from the very beginning it was never denied that socialism could solve the calculation problem in equilibrium.[44] Thus, socialism now, as then, is to be judged under the conditions of the real world.

As a natural follow-up to the above digression, before the rules regarding price, cost and quantity are analyzed, we can study socialism on the disequilibrium plane. Disequilibrium in the socialist system consists of shortages and surpluses that present themselves under changed conditions.

To Lange, these moments of disequilibrium present little cause for concern. They appear, are diagnosed and are eliminated by "small adjustments" in price by the CPB.[45] Then normality returns. The process is described as "simple" and the correction time "much shorter" than under capitalism.[46]

Mises has forcibly denied the simplicity of such a procedure on the grounds of the static-dynamic squabble just discussed. Trial and error, explains Mises, is a strategy which assumes that the thing "one is looking for remains unchanged during the trial (such as searching for a misplaced wallet)."[47] In other words: "The method of trial and error is applicable in all

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cases in which the correct solution is recognizable as such by unmistakable marks not dependent on the method of trial and error itself."[48] In contrast, "Things are quite different if the only mark of the correct solution is that it has been reached by the application of a method considered appropriate for the solution of the problem."[49]

Mises' argument can be complemented by two separate discussions: the first dealing with economic change and the second examining the nature of correcting individual prices.

When Lange explains the "trial and error" technique, one is immediately impressed with the banishment of change in his system.[50] Such statements as "so the process goes on until the objective equilibrium condition is satisfied and equilibrium finally reached" remind one more of natural scientists in the laboratory than applied economists checking inventory. The weakness of this, as Hoff has observed, is that "the advocates of the 'trial and error method' obviously assume that the community will be static, and expect that conditions will remain unaltered while the 'trial' is being made."[51] And, when one assumes that the adjustments are accompanied by drifts in other price-influencing factors, the "correction" becomes not only tentative, but *too late*. This leads us to a vital and neglected (by the neoclassicists and market socialists) distinction in economic functions—managerial adjustment versus entrepreneurial alertness. We will pursue this area in the next section of the paper. There is a second major weakness in the Langian method for achieving scarcity prices that even the Austrians underemphasize.

The success the market socialists hope to find cannot be attained with only a price being "right" (e.g., where supply and demand mesh, preventing surpluses or shortages). The price interrelationships must also be accurate. This means that to monitor and judge any particular price, one is assuming that its substitutes and complements are in balance, preventing any falsifications in the monitored price's demand. For example, if good A has a price equating supply and demand, while its substitute B is out of equilibrium, then A's price is transmitting misinformation though equilibrating. And to "correct" the price of B would be to upset A's equilibrium. Further, it is logically possible that a good and its substitutes all have equilibrating prices, yet their prices not be indices of true scarcity. In this case, the bad prices merely camouflage each other. So we can see that monitoring individual prices is not enough; the CPB would have to be in command of *all* price interrelationships. Thus the "trial and error" method becomes inadequate since it only applies to prices individually.

Part V: Entrepreneurial Alertness Versus Managerial Adjustment

Though not schooled in the Austrian tradition, Harvey Leibenstein has expressed this school's disenchantment by saying: "If we want to get anywhere to solve the entrepreneurial puzzle, we have to stay away from the

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neoclassical general equilibrium syndrome."[52] And, just like the neoclassical school Leibenstein chides, the market socialists also see entrepreneurship as a nonspecific talent, easily duplicated by bureaucratic management and CPB corrections. Such casual asides by Lange as "the process of price determination is quite analogous to that in a competitive market" demonstrate this point.[53]

In Austrian theory there is more than producers and consumers who adjust their actions to one another; there is also the entrepreneur, characterized by his alertness to "differences between the sum of the prices of the complementary factors of production and the prices of the (final) products."[54] These discrepancies offer both profit and loss to those combatting these gaps of knowledge in the face of uncertainty.[55] So we can see the activity of the entrepreneur in the market as necessary, since error must exist in factor prices and final products, and also positive, since eliminating these discrepancies provides equilibration. And as this process never stops, the entrepreneurial function is continuous.[56]

The entrepreneurial function obviously goes beyond the framework of "*given*" ends and means to which Lange refers throughout his article.[57] Ironically, it was the critic of socialism Lionel Robbins, in his 1932 *Essay on the Nature and Significance of Economic Science*, who couched the economic problem in terms of *givens*,[58] thus providing a methodological basis for the market socialists' view of the economic problem. We must interpret such a view as limited since:

> Robbinsian decision-making presupposes that the framework has already been set up. [But] it is precisely the "entrepreneurial" element responsible for setting up the Robbinsian framework which is not itself a factor in the economizing decision. . . . [Yet] there is nothing in the calculative activity of which Robbinsian decision-making consists which calls for deliberately out-distancing one's fellow market participants.[59]

As against the overly narrow concept of economizing, there is Misesian *human action* (or rivalry). The latter concept, with regard to efficiency, includes not only economizing but also the benefits of change—new products, innovations in old products and the abandonment of past "givens". After all, there always exist things which consumers do not know about but would prefer. And it is here that the entrepreneur comes into his own by locating and acting upon price discrepancies that alert him to unfulfilled wants.

The above explication of entrepreneurship should bring to light the anticipatory nature of its function. He anticipates what future conditions hold and is penalized or rewarded in his quest for profits.[60] Conversely, the "trial and error" CPB corrector passively reacts to over-and-done-with situations and does not actively anticipate with "his" resources.[61] Such reacting to error is obviously less efficient than fighting error ahead of time.

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It should be pointed out that the bureaucrat cannot play the role of entrepreneur. Entrepreneurship requires a market and privately raised capital. Notes Mises, "The quality of being an entrepreneur is not inherent in the personality of the entrepreneur; it is inherent in the position which he occupies in the framework of market society."[62] In this sense, we cannot have "government on a business basis", i.e., treat tax allocations as market revenue or treat any surplus over cost as profit.[63]

The explanations, arguments and points made in this section of the paper can be re-emphasized by quoting Professor Kirzner at length:

> The crucial question for government-market comparisons must concern the capacity of each of the two systems *to bring available opportunities to the attention of decision-makers*. Even if the costs to government of reallocating resources were zero, and even if this included the costs of acquiring information, it would not follow that in a government-directed economy resources would inevitably be optimally allocated. To make this conclusion valid we would have to assume not merely that government could acquire information costlessly, but that government was already omniscient. A market relies on the incentive of profit to set into motion the entrepreneurial process. It is solely because of the desire to obtain profits that we can, in any degree, "rely" on entrepreneurial discovery of where profits are to be had. Under government direction, it is not at all clear what substitutes for the profit incentive are available, in the absence of omniscience—not merely to spur the exploitation of socially desirable opportunities, but to direct attention to their very existence. Only if we ignore the role played by this entrepreneurial element can we fail to raise the question of a corresponding role in the government-directed economy.[64]

Part VI: The Weaknesses of Bureaucratic Management

At this point in the paper we may approach the above-mentioned weaknesses of market socialism in less technical terms by contrasting profit/loss with bureaucratic management. Interestingly enough, bureaucracy is a bad word to socialists of all stripes. Lange admits that "the real danger of socialism is that of bureaucratization of economic life."[65] Lippincott agrees.[66] Assar Lindbeck, in a sympathetic study of the New Left, similarly notices that the New Left is critical of bureaucracy and quotes the distinguished Marxist Ernest Mandel to this effect.[67]

What are the economics of bureaucracy?

The bureaucracy must, above all, provide the designated good or service. Of secondary importance is the cost of such an operation. In contrast, for the entrepreneur the turning of a profit is invariably linked to the operation itself. Therefore, costs tend to be higher for the former than the latter. Furthermore, while the bureaucracy can obtain its operating money by compulsory taxation, the entrepreneur must demonstrate the

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worth of his project to potential capitalists. This channels scarce capital to the most skilled entrepreneurs, encouraging a maximum utilization of resources not present under bureaucracy.[68]

An important point made in a previous section regarding innovation under socialism has been stated by Professor Rothbard regarding bureaucracy:

> Inventions, innovations, technological developments, by their very nature, by definition, cannot be predicted in advance and therefore cannot be centrally and bureaucratically planned. Not only does no one know what will be invented when; no one knows who will do the inventing.... Bureaucracy, incompetent enough to plan a stationary system, is vastly more incompetent at planning a progressive one.[69]

Before extending the analysis of market socialism to the rules (see Part VII), one can profitably point out several other weaknesses of replacing market processes with public ownership. One such limitation is the speed with which information can be utilized.[70]

Change under the Lange system encounters mandatory procedures such as the CPB audit and political permission before a new course of action may be embarked upon.[71] (And, as discussed above, the change is always too late if the trial conditions have changed in the meantime.) Conversely, in a free market, changing conditions are anticipated and acted upon without delay, for profit-making is characterized by acting on private knowledge before it is known by others. For instance, it is not enough to know that company *A* will have a better demand for its products; one must act on this knowledge before it is enough well-known by others to alter present conditions therefore removing the profit opportunity.

Under capitalism, the operations of the futures and stock markets efficiently register *instantaneous* adjustments in information.[72] Importantly, *expectations* are fully utilized under such institutions, promoting a highly economic usage of society's capital stock under changing conditions. It is a curious yet understandable fact that expectations as a guide to allocative efficiency have been so thoroughly demoted in the socialist schemes.

Part VII: The Production Rules of Market Socialism: A Critique

With "trial and error" giving prices meaning, it will be remembered, efficiency is attempted under market socialism by pricing at marginal cost and producing at minimum average cost.[73] We may briefly review the shortcomings of such a procedure.

First of all, these rules have their rationale in the equilibrium world of perfect knowledge and perfect factor divisibility and outside of it lose their authority. But efficiency in *disequilibrium*, contrarily, is to minimize error and *revise plans* toward an *attainable* optimum.[74] Related to this, Hayek

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has impressively attacked the above conditions of omniscience as the solution to the "economic problem," as we have examined.[75] Mises, in his original article on socialism, made essentially the same point when he spoke of "a kind of intellectual division of labor."[76]

Also, regarding the production rules, we must make the point that *costs are not objective and "given", but subjective and known only to the "man on the spot."*[77] And, as Hayek and others have noticed, costs depend on many things *besides* prices in the production period.[78] The labor theory of value notwithstanding, once something is produced, costs are bygones and sunk and prices are anticipations. Also, before production, costs are themselves anticipations. Yet, as in the previous section, we must ask where risk and anticipation fit in the market socialists' plans, and how an outsider (the CPB auditor) can determine the costs and/or assess responsibility.[79]

The subjectivist revolution of a century ago established value as subjective. But, if value is subjective and nonmeasurable, then so, too, are costs since cost is the *value* placed on the most attractive opportunity forgone. The theory of subjective costs, so well formulated by von Wieser, and then extended by Thirlby, Wiseman, Robbins, Hayek and Coase in the 30's and 40's,[80] has also been grasped by economists outside of this tradition. The general equilibrium economist J. de V. Graaf abandons the P = MC rule, concluding that "the conditions which have to be met before it is correct (welfare maximized) to set price equal to marginal cost in a particular industry are so restrictive that they are unlikely to be satisfied in practice."[81] And P. C. Roberts has noticed that:

> under real world conditions characterized by the passage of time, the marginal rule gives no clear guidance to those directed to organize production in accordance with it. Introducing the element of time brings in uncertainty and requires the exercise of *judgment*. Neither uncertainty nor judgment is present in the formulation of perfect competition from which Lange took his idea of the marginal rule.[82]

Lastly, this rule, in replacing profit/loss, does away with the market's test of success which allocates capital to its most competent users, with the will to cut costs, and with the most reliable incentive for equilibration. These deprivations must be deplored.

The other key rule, producing at minimum cost, is particularly subjective and question-begging. This rule, unmasked, is simply a euphemism for "doing the best you can," overlooking the *conditions* for cost minimization. Under capitalism such conditions *do* exist. Each firm has an outside market to judge whether or not it should produce or buy a factor, and all firms tend toward plant size optimality. And, as we have emphasized throughout this paper, "the opportunity for anybody who knows a cheaper method to come in at his own risk and to attract customers by underbidding the other producers" is omnipresent.[83] Socialism, to the contrary, does not have an institutional framework offering these processes and consequently will not

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be able to discover least-cost combinations for production. Passing a law enforcing this rule cannot nullify this void and is therefore doomed to ineffectiveness.

In examining the rules of market socialism, we should lastly analyse whether it truly preserves consumer sovereignty.

Realizing that all production depends on final consumption for its value, the socialists have readily allowed consumer tastes to direct their economy. But, as Hayek and others have pointed out regarding the direction of productive activity, the wishes of the CPB and the wishes of the consumer cannot concurrently prevail.[84] So, in reality, under socialism consumers can merely do the best they can ("minimizing their losses"), "freely" buying only the things that the powers at large have authorized, rather than freely buying from the constantly changing "menu" which entrepreneurs can offer.[85] Consumer sovereignty, as the term was used by W. H. Hutt, applies in its fullest sense, then, only to the market economy.

A similar situation exists regarding the alleged sovereignty of labor over their employment opportunities. The state sanctions all jobs and *then* its citizens choose. And even then the rewards for labor are manipulated to achieve a "social optimum."[87] All in all, one is left with the impression that freedom exists in name only.

Part VIII: The "Advantages" of Market Socialism

Our final section censuring market socialism must deal with its "advantages" over market capitalism. After all, Lange does not wish only to duplicate the market but to correct its perceived shortcomings.

One such "improvement" is to replace capitalism's monopolistic elements with "perfect competition," thus "add[ing] a much more powerful argument to the economist's case for socialism."[88] In response to this claim, we have demonstrated that such a static view of optimality cannot be a criterion for real world adjustment. One cannot even imagine a world of perfect knowledge, perfect factor divisibility, zero information costs and objective costs. The Austrian theory of dynamic adjustment via the profit-seeking entrepreneur provides a much superior normative concept. It is the entrepreneur that performs a vital social function in a world containing error.

Superiority is also claimed by Lange in that the CPB can "maximize social welfare [by] taking all the alternatives into the economic account.[89] (This includes equating social costs and benefits.) There are a number of fallacies here. One such error is the illegitimate jump from an individual's welfare to that of society. One must never forget that the Pigovian concepts of "social costs" and "social benefits" are meaningless if value and cost (itself a value) are subjective. To try to employ any unit or standard for addition or comparison is mere intellectual play. The second problem with

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Lange's claim is his assumption that the CPB is in a better position to obtain information than a decentralized market is. We have dealt with this earlier and refer the reader to Hayek's classic essay "The Use of Knowledge in Society," of 1945.

A final significant advantage claimed for socialism is the promised taming of the business cycle since "mistakes can be localized, [and thus] a partial overproduction does not need to turn into a general one." Yet, by not specifically outlining a market socialist monetary policy, Hayek has countered this argument by saying the socialists have not given us the needed information about their promise.[90]

Part IX: Conclusion

This essay has been an attempt to string together the far-ranging criticisms of market socialism, laying to rest the widespread belief that, while the insights of Austrians were valid against Marxian socialism, they lose their theoretical sting against market socialism. Rather, we have demonstrated that the arguments significantly overlap, this fact being obscured by the market socialists' hiding behind the neoclassical smokescreen of "pure and perfect competition."

One point should emerge from all this: that to fully appreciate the insights of Mises, Hayek, Kirzner, Rothbard and Lachmann—the modern-day Austrians—against market socialism, one must understand modern subjectivist economics. Indeed, all of our arguments in this paper stem from the key insight that all human perceptions of the objective world are subjective. Conversely, to take certain insights of this school (e.g., the function of money prices for Mises or the complexity arguments of Hayek) and then to work within the neoclassical framework is to lose one's perspective on the entire debate. And to lose one's perspective is to join orthodoxy in its verdict that the Austrians were refuted by the socialists' revisions made in response to Mises' original article.

NOTES

1. F. A. Hayek, "The Nature and History of the Problem," in Hayek, ed., *Collectivist Economic Planning* (London: George Routledge and Sons, 1935), p. 32.
2. Ludwig von Mises, "Economic Calculation in the Socialist Commonwealth," in Hayek, *Collectivist Economic Planning*, p. 111.
3. Mises, *Die Gemeinwirtschaft* (1922), reprinted under the title *Socialism: An Economic and Sociological Analysis*, trans. J. Kahane (New Haven, Conn.: Yale University Press, 1969).
4. Hayek, "The Nature," p. 36.
5. Oskar Lange, "On the Economic Theory of Socialism," in Benjamin F. Lippincott, ed., *On the Economic Theory of Socialism* (1938; New York: McGraw-Hill, 1964), p. 57.
6. Our discussion of neoclassicism as being the "heritage" of the market socialists is somewhat novel. Usually, the neoclassical economists are embedded within the theory of capitalism. Far better, Carl Menger should be the link between Adam Smith and the modern-day Austrians (Mises and Hayek) in the theory of capitalism.

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7. Leon Walras, *Elements of Pure Economics* (1874; London: George Allen and Unwin, 1953).
8. Vilfredo Pareto, *Manuel d'economie politique* (1927), p. 354.
9. Enrico Barone, "The Ministry of Production in the Collectivist State," in Hayek, *Collectivist Economic Planning*, pp. 245–90.
10. Lange is not unaware of this. In large part, he attributes his solutions to Walras' *tâtonnements* and Barone's equations. See Lange, "On the Economic Theory," pp. 64, 70.
11. *Ibid.*, p. 73.
12. *Ibid.*, p. 79.
13. *Ibid.*, p. 83.
14. *Ibid.*, p. 84. This restraint may seem inconsistent with the above freedom to take the highest wage.
15. *Ibid.*, pp. 75–76.
16. See Fred M. Taylor, "The Guidance of Production in a Socialist State," in Lippincott, *On the Economic Theory*, pp. 48–50; and Lange, "On the Economic Theory," p. 76.
17. *Ibid.*, p. 77.
18. *Ibid.*, p. 75.
19. *Ibid.*, p. 77.
20. *Ibid.*, p. 75.
21. See Taylor, "The Guidance of Production," pp. 51–54.
22. Lange, "On the Economic Theory," p. 87.
23. *Ibid.*, pp. 86–87.
24. *Ibid.*, p. 93.
25. *Ibid.*, p. 97.
26. *Ibid.*, pp. 81, 93.
27. *Ibid.*, p. 94.
28. *Ibid.*, p. 85.
29. *Ibid.*, p. 107.
30. It will be remembered that Lerner was one of the so-called "Big Four" in Hayek's seminar at the London School of Economics along with Lionel Robbins, J. R. Hicks, and Nicolas Kaldor. Ludwig Lachmann was another notable member of this early-1930's group.
31. Abba P. Lerner, "Statics and Dynamics in Socialist Economics," *Economic Journal* 47 (June 1937): 254. Lerner elsewhere criticizes Lange's equilibrium since he "takes the state of competitive equilibrium as his *end* while in reality it is only a means to the end." To aim at the ideal, continues Lerner, is different from being there, and in disequilibrium the P=MC optimality is not what it is in equilibrium. (Lerner, "A Note on Socialist Economics," *Review of Economic Studies*, vol. W [October 1936]: 74).
32. Lange, "The Computer and the Market," in C. H. Feinstein, ed., *Socialism, Capitalism and Economic Growth* (Cambridge: Cambridge University Press, 1967), pp. 158–59. Also notice Jan Drewnowski's statement that "Mises, as everybody agrees now, was wrong in his main contention. . ." (Drewnowski, "The Economic Theory of Socialism: A Suggestion for Reconsideration," *Journal of Political Economy* 69, no. 4 [August 1961]: 341).
33. One should not overlook T. J. B. Hoff, *Economic Calculation in the Socialist Economy* (London: William Hodge, 1949), a valuable summation of the debate from the Misesian perspective.
34. "The capitalist economy today is as far from the pure ideal of the economic theorist as it is from a socialist economy" (Lippincott, "Introduction," in Lippincott, *On the Economic Theory*, p. 25).
35. Hayek, "The Meaning of Competition," *Individualism and Economic Order* (1948; Chicago: Henry Regnery Company, 1972), p. 92.
36. Lachmann has insightfully raised this point: "Unfortunately, the Pure Logic of Choice [Hayek's term for equilibrium] has filled the minds of economists to such an extent that the study of the actual means and ways by which men try to realize their aims has come to be sadly neglected. Economists, not unnaturally, prefer to do field-work in a pleasant green valley where the population register is exhaustive and everybody is known to live on either the right or the left hand of an equation. Only on rare occasions—and scarcely on

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their own free will—do they embark on excursions into the rough uplands of the World of Change to chart the country and to record the folkways of its savage inhabitants; whence they return with grim tales of horror and frustration" (Ludwig M. Lachmann, "The Role of Expectations in Economics," *Capital, Expectations, and the Market Process*, ed. Walter E. Grinder [Kansas City: Sheed Andrews and McMeel, 1977], p. 70).

37. Hayek, "The Meaning of Competition," p. 95.
38. *Ibid.*, pp. 96–101.
39. Kirzner, *Competition and Entrepreneurship* (Chicago: The University of Chicago Press, 1973), pp. 97–99.
40. For an informative history of the two different approaches to competition beginning with the classical school, see Paul McNulty, "Economic Theory and the Meaning of Competition," *Quarterly Journal of Economics* (November 1968); and *idem*, "A Note on the History of Perfect Competition," *Journal of Political Economy* (August 1967).
41. Hayek refers to this "Turn[ing] economics into a branch of pure logic...a sort of Pure Logic of Choice" ("Economics and Knowledge," *Individualism and Economic Order*, p. 35 and passim).
42. F. H. Hahn, "On Some Problems of Proving the Existence of an Equilibrium in a Monetary Economy," in R. W. Clower, ed., *Monetary Theory: Selected Readings* (Baltimore: Penguin, 1969). Also see Mises, *Human Action* (1949; Chicago: Henry Regnery Company, 1966), p. 250.
43. Hayek, "Economics and Knowledge," p. 33. For recent attacks on the misplaced emphasis on equilibrium, see Kirzner, *Competition and Entrepreneurship*; G. L. S. Shackle, *Epistemics and Economics* (Cambridge: Cambridge University Press, 1973); and Brian Loasby, *Choice, Complexity and Ignorance* (Cambridge: Cambridge University Press, 1976).
44. As Mises remarked, "The static state can dispense with economic calculation....But this is only conceptually [read theoretically] possible" (Mises, "Economic Calculation in the Socialist Commonwealth," p. 109). If this point were better understood, the confusion over the "second line of defense" regarding the theoretical and practical would evaporate. This caused Mises to later remark in his autobiography, "They failed to see the first challenge..." (*Notes and Recollections* [South Holland, Mich.: Libertarian Press, 1978], p. 112).
45. Lange, "On the Economic Theory," p. 86.
46. *Ibid.*, p. 89. In contrast, Shackle writes: "The number of distinct trials, even if confirmed to discrete steps of price and quantity, would be so immense that the necessary 'market day' would extend beyond human lifetimes" (*Epistemics and Economics*, p. 150).
47. Mises, *Human Action*, pp. 704-705.
48. *Ibid.*, p. 704.
49. *Ibid.*
50. The present writer can only echo the words of Arrow's recollection: "Even as a graduate student I was somewhat surprised at the emphasis on static allocative efficiency by market socialists..." (K. J. Arrow, "Limited Knowledge and Economic Analysis," *American Economic Review* 64 [March 1974]).
51. Hoff, *Economic Calculation in the Socialist Society*, p. 81. Also see Armen Alchian, "Uncertainty, Evolution and Economic Theory," *Economic Forces at Work* (Indianapolis, Ind.: Liberty Press, 1977), pp. 30–31. For the same argument employed against using differential equations for problem solving, see Lionel Robbins, *The Great Depression* (1934; Plainview, N.Y.: Books for Libraries Press, 1976), p. 151.
52. Harvey Leibenstein, as quoted in *Center for Applied Economics Newsletter* (New York University, February 1978), p. 2.
53. Lange, "On the Economic Theory," p. 82. Two pages later he again makes this very statement. His obliviousness of the entrepreneurial function is obviously crucial to his case.
54. Mises, *Human Action*, p. 290. Mises' entrepreneur should not be confused with Knight's "residual claimant" innovator. While Knight's gain is an unexplained windfall, a return to uncertainty from being in the right place at the right time, Mises' entrepreneurial return stems from correct foresight of a future unlike the present and acting on it. (See Frank H.

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Knight, *Risk, Uncertainty and Profit* [1921; Chicago: University of Chicago Press, 1971]). Mises' theory is also distinct from Schumpeter's and Bronfenbrenner's. (See Kirzner, *Competition and Entrepreneurship*, pp. 75–87.)

55. The assumption here is that if everyone possessed perfect knowledge, there would be no profits (undercapitalization of factors) or losses (overcapitalization of factors). See Murray N. Rothbard, *Man, Economy and State* (Los Angeles: Nash Publishing, 1970), p. 483. Thus, the entrepreneur does not exist in equilibrium.
56. "Our reflection is thus that the market is a continuous process without beginning or end. Marshallian markets for individual goods may, for a time, find their respective equilibrium. The economic system never does. This process is propelled by equilibrating forces of intermarket interaction which are, again and again, thwarted by changes in the pattern of the distribution of knowledge" (Lachmann, "Austrian Economics in the Present Crisis of Economic Thought," *Capital, Expectations and the Market Process*, pp. 39–40).
57. The starting point of market socialism is to use historical prices, obviously "given." Lange further compares and contrasts his schemes with capitalism, both under *given* conditions. Lange, "On the Economic Theory," pp. 60, 67–68, 72–73, and passim.
58. Robbins writes: "the subject matter of economics is . . . conditioned by the scarcity of *given* means for the attainment of *given* ends" (*An Essay on the Nature and Significance of Economic Science* [London: Macmillan, 1932], p. 46).
59. Kirzner, *Competition and Entrepreneurship*, pp. 95–96.
60. We might add that this is for the Austrians what "trial and error" is for the socialists.
61. If he worked under static conditions, we could make a case for the adjustment being "anticipatory."
62. Mises, *Bureaucracy* (New Rochelle, N.Y.: Arlington House, 1944), p. 49.
63. See Mises, *A Critique of Interventionism* (1929; New Rochelle, N.Y.: Arlington House, 1977, pp. 158–62.
64. Kirzner, *Competition and Entrepreneurship*, p. 230.
65. Lange, "On the Economic Theory," p. 109. We cannot agree, however, that this is a "sociological" problem.
66. Lippincott, "Introduction," *On the Economic Theory*, p. 37.
67. Lindbeck, *The Political Economy of the New Left: An Outsider's View* (New York: Harper & Row, 1971), pp. 32–33.
68. For an excellent discussion of these and other points, see Mises, *Bureaucracy* (New Haven, Conn.: Yale University Press, 1944), chaps. 1 and 2.
69. Rothbard, *Man, Economy and State*, p. 832.
70. See Hayek, "The Use of Knowledge in Society."
71. "The S.E.C. [C.P.B.] will be able to act only after the parties have reported, the reports have been verified, contradictions cleared up, etc.; and the new prices will become effective only after all the parties concerned have been notified. . ." (Hayek, "The Competitive 'Solution,'" *Individualism and Economic Order*, p. 148). Also see Abram Bergson.
72. "The Stock Exchange is perhaps the most characteristic of all the institutions of the market economy. . . . What really distinguishes [capitalism] from a socialist economy is not the size of the 'private' sector of the economy, but the ability of the individual freely to buy and sell shares in the material resources of production. Their inability to exercise their ingenuity in this respect is perhaps the most important disability suffered by the citizens of socialist societies, however large their incomes may be, however wide the range of consumption goods that may be available to them" (Lachmann, "Methodological Individualism and the Market Economy," *Capital, Expectations and the Market Process*, p. 161).
73. Of course, if our previous arguments against "trial and error" pricing are adopted, then cost as a guide to production loses its economic significance since costs *are* prices.
74. As Lachmann reminds us, the entrepreneur "has another function which we all know about but which little is, as a rule, heard from economists: the 'regrouping of capital assets' by buying and selling them, the incessant reshuffling of the combinations of complementary capital goods with which he works and which in their complexity form the ever-changing basis of the capital structure" ("The Science of Human Action," *Capital, Expectations and the Market Process*, pp. 104–105).

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75. As Hayek states: "The peculiar character of the problem of a rational economic order is determined precisely by the fact that the knowledge of the circumstances of which we must make use never exists in concentrated or integrated form but solely as the dispersed bits of incomplete and frequently contradictory knowledge which all the separate individuals possess. The economic problem of society is thus not merely a problem of how to allocate 'given' resources—if 'given' is taken to mean given to a single mind. . . . [Rather] it is a problem of the utilization of knowledge which is not given to anyone on its totality" (Hayek, "The Use of Knowledge in Society," pp. 77–78).
76. Mises, "Economic Calculation in the Socialist Commonwealth," p. 102.
77. Hayek, "The Use of Knowledge in Society," p. 84.
78. Hayek, "The Competitive 'Solution,'" p. 198.
79. *Ibid.*
80. See the collection of essays compiled by James Buchanan in his *L. S. E. Essays on Costs* (London: Weidenfeld and Nicholson, 1973). Also see R. H. Coase, "The Marginal Cost Controversy," *Economica* (August 1946); and G. F. Thirlby, "The Marginal Cost Controversy: A Note on Mr. Coase's Model," *Economica* (February 1947).
81. J. de V. Graaf, *Theoretical Welfare Economics* (Cambridge: Cambridge University Press, 1957), p. 154.
82. Paul Craig Roberts, *Alienation and the Soviet Economy* (Albuquerque, N.M.: University of New Mexico Press, 1971), p. 97, as quoted in Rothbard, "Ludwig von Mises and Economic Calculation under Socialism," in Laurence S. Moss, ed., *The Economics of Ludwig von Mises: Toward a Critical Reappraisal* (Kansas City: Sheed and Ward, 1976), p. 73.
83. Hayek, "The Competitive 'Solution,'" p. 196.
84. This is particularly true when it is realized that the planners "arbitrarily" decide the ratio of present to future consumption—the "social rate of growth." See *ibid.*, p. 204. The incompatibility of freedom and planning has been forcibly argued by Hayek elsewhere. See his *The Road to Serfdom* (Chicago: The University of Chicago Press, 1944), esp. chaps. 5–8. Also see Rothbard, "The Myth of Democratic Socialism," *Libertarian Review* 6 (September 1977): 24–27.
85. The socialist "should remember that consumer sovereignty means more than the passive acts of consumers to make the best of an unappealing menu of choices. Economic democracy is not achieved unless consumers' preferences count in determining output in the first place" (W. H. Loucks and W. G. Whitney, *Comparative Economic Systems*, 9th ed. [New York: Harper and Row, 1973], p. 187).
86. See W. H. Hutt's classic article, "The Concept of Consumers' Sovereignty," *Economic Journal* (March 1940), pp. 66–77. As an analogy of the socialists' misuse of the term, we could say that a prisoner is still free since he still has a (limited) range of activities from which to choose without coercive interference.
87. Lange, "On the Economic Theory," p. 83.
88. *Ibid.*, p. 107.
89. *Ibid.*, p. 106.
90. Specifically the socialists do not tell us about their monetary policy, and this is the key matter to those who, like Hayek and Mises, hold a monetary theory of the trade cycle. See Hayek, "The Competitive 'Solution,'" p. 207.

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A Critique of the Standard Account of the Socialist Calculation Debate

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As the Marxian philosopher Louis Althusser used to put it, no reading is innocent. The meaning a reader derives from a particular piece of scholarly literature is unavoidably influenced by his premises and analytical framework. When the underlying theoretical framework of the reader differs sharply from that of the writers under examination the result is likely to be profound misunderstanding. Few instances of "non-innocent" reading can match the distortion that the standard account of the socialist calculation debate has imparted to that famous controversy. Many of the most influential early readers of the debate later corrected at least part of their initial errors of interpretation. However, the version of the history of thought of the debate that has come to dominate the profession still retains most of those initial errors. This essay will survey the origins and development of the standard view of the socialist controversy, offering suggestions along the way about how and why this interpretation seriously misreads some of the arguments of the debate.

The two sides of this controversy can be designated as the "Austrians" who issued the challenge to socialism—notably Ludwig Mises, Friedrich Hayek and Lionel Robbins[1]—and, on the opposite side, the "neoclassicals" who defended one form or another of socialism from this challenge—primarily the so-called "market socialists" Oskar Lange, H. D. Dickinson, Fred M. Taylor, Abba P. Lerner, and E. F. M. Durbin, and, from a somewhat different point of view, Maurice Dobb.[2]

The entire debate concentrated on attempts to answer the initial challenge by Mises that rational central planning of the vast and complex modern economy would be "impossible." Without private ownership of the means of production, he argued, there could be no competitive market for these capital goods, and without markets, there could be no prices for the various scarce means of production. Lacking the guide of market prices, the central planners would be "in the dark" as to the *relative* scarcity of different components of the capital structure and so would invariably fail to combine and use them efficiently.

The famous "market-socialist" response by Lange is generally under-

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stood to have effectively answered Mises by first admitting the indispensability of "markets" and "prices," and by then arguing that these could be reconciled with "public" or "common" ownership of the means of production. Lange considered the Walrasian simultaneous-equation formulation that had been advanced by Enrico Barone in 1908 to be a rigorous and conclusive answer to Mises' claim that socialism was "theoretically impossible." He invoked Fred Taylor's "trial and error" method[3] as a refutation of the Hayek-Robbins thesis that socialism, though theoretically possible, was impracticable.

However, this entire elaborate answer to the Austrian challenge is premised upon a particular neoclassical reading of that challenge. Clearly if, as this paper contends, the neoclassicals, including Lange himself, fundamentally misunderstood the Austrian challenge they are supposed to have refuted, the challenge ought to be considered anew. However, before we can confidently embark on such a reconsideration, we should attempt to offer a plausible explanation of how the economics profession came to misunderstand the calculation debate so thoroughly.

This misunderstanding, we will argue, is rooted in basic differences between the "Austrian" and "neoclassical" paradigms which were not yet evident to either side at the time of the debate, but which have since become clarified, especially in Professor Kirzner's Austrian critique of neoclassical choice theory.[4] These implicit differences made it easy for neoclassical participants and readers of the debate to attach inappropriate neoclassical meanings to the concepts the Austrians were employing. In particular the concepts "economic theory" (misunderstood to mean static equilibrium theory), "efficiency" (mistaken for "Pareto optimality"), "ownership" (taken to mean formal legal title, rather than *de facto* control, over resources), and "competition" (read as the state of perfect competition rather than as a process) were "lost in the translation" by the neoclassical historians of thought of the debate.

We begin by outlining (1) the major elements of the standard account of the debate, documenting in footnotes that this interpretation thoroughly permeates contemporary economics, and (2) contrasting elements of what we will call the "alternative" interpretation. We will then conduct a critique of this standard account, selecting seven representative interpreters of the debate (including some of the most respected scholars in economics) for analysis. It will be our contention that, despite the accumulated weight of scholarly authority associated with such names as Joseph Schumpeter, Abram Bergson, Benjamin Ward, and Frank Knight, this prevailing interpretation ought to be rejected in favor of an alternative, "revisionist" interpretation which carries the authority of a rather less famous name like that of Trygve Hoff.[5] It would seem that this is an ambitious enough task for one paper; thus it is hoped that we will be forgiven for not venturing to offer a thoroughgoing reexamination of the calculation debate from this

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alternative perspective. We only intend to demonstrate that the generally accepted view of the debate is riddled with errors and thus urgently requires such a thorough reexamination.

The Two Interpretations of the Debate in Outline

1) *The Standard Account of the Debate*

a) *pre-1920:* Before the debate, it is generally agreed, very little attention had been paid to the economics of socialism.[6] Much of what did exist in such literature failed to realize that some form of market prices and some use of money were indispensable for rational planning. The failure of the War Communism period in the Soviet Union is often cited as evidence that many early socialists erred in underestimating the importance of prices for central planning.[7] The view is occasionally expressed that in actuality this conception of socialism without prices was a straw man fabricated by Mises and Hayek and that it was never seriously held by socialists.[8] The more common view, however, is that at least some early socialists had to be taught their economics by neoclassical economists. In any case, few modern socialists believe that prices, money, and markets (at least for consumer goods and labor) can be dispensed with until scarcity itself is eliminated.[9]

b) *Mises:* Mises' calculation argument is generally credited with having shaken socialists out of their neglect of the economics of planning, but few commentators on the debate are willing to grant him much more than this stimulative accomplishment.[10] His argument is usually interpreted in neoclassical terms, as a denial of the "logical credentials" of socialism,[11] and thus as an assertion that rational economic calculation is not only "impracticable," but also "theoretically" impossible without private ownership of the means of production, even under static conditions.[12] Some discussants say that the practical experience of socialist planning in the USSR refutes Mises' claim,[13] many claim that either Lange's or Barone's argument conclusively counters Mises', but there is a remarkably wide consensus that he was wrong.[14]

c) *equation-solving:* It is generally held that, before Mises issued his challenge, Barone's equilibrium argument had already established the "theoretical" possibility of socialism by showing that in principle the Central Planning Board (CPB) could solve a set of simultaneous equations, in much the same way as is done in practice by the market. The same general equilibrium logic of choice which Walras had developed to analyze capitalism could be applied to socialism.[15]

d) *impracticability:* The view is common that Hayek's and Robbins' arguments were substantially different from Mises', constituting a retreat to the acceptance of the theoretical possibility, but a denial of the practicability of socialism. The essence of their argument is taken to

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be that solving Barone's equations is not feasible as a method of central planning.[16] Hayek is sometimes also credited with having raised some important issues concerning the centralization of knowledge, risk, and managerial incentives, though these are generally held as considerations to be taken into account by central planners rather than as arguments against central planning.

e) trial and error: It is widely held that the market-socialists, particularly Lange, met Mises on his own terms[17] and thoroughly proved that Mises and his school were wrong.[18] They demonstrated that a determinate equilibrium can be defined for socialism as Barone had shown, and that, contrary to Hayek and Robbins, the CPB could "find" this equilibrium set of prices by a process of trial and error. Thus it is claimed that socialism is practicable in principle.[19]

f) conclusion: The implication that is usually drawn from the debate is that economic theory *per se* cannot decide the great controversy between capitalism and socialism. Neither system is as praiseworthy in practice as the debaters depicted them in theory.[20] The efficiency criteria of the debate were developed under strictly static welfare assumptions,[21] while under more realistic, non-static assumptions neither system can boast the virtues of Pareto-optimality.[22] Most economists agree that there are strengths and weaknesses of each system. Some stress that market-socialism has the potential of improving upon capitalism;[23] others emphasize that, though socialism is theoretically unassailable, it nevertheless has other, major deficiencies deemed to be outside the province of economic theory, notably the danger of bureaucratization.[24] Most economists criticize both sides of the famous controversy for dealing on too abstract a level and for comparing the idealization of one system with the practical weaknesses of its opposite.[25] A related reaction to the debate is the argument that the participants focused too much on alternative "Isms," that the controversy was a stale quarrel over unworkable extremes—"plan *vs.* market"—while contemporary economists agree that both institutions are indispensable.[26] Modern dispute is only over the proper mix of the two.[27]

g) beyond the debate: The most significant element in the standard account of the calculation debate is the view that the debate was marred by its exclusive attention to "statics." Two of the major subsequent developments in socialist economic theory can be understood as differing attempts to advance central planning theory beyond this static equilibrium context. Thus one branch of modern socialist economics, "planometrics," seeks to produce mathematical procedures for getting prices to approach their equilibrium values, as against the debate's focus on formal conditions for static equilibrium.[28] Another branch, which we will call "macroplanning," seeks to examine ways to

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control and improve the overall growth rate of the economy and to influence the direction of new investment in broad macroeconomic categories of production toward this end, as against the debate's emphasis on static microeconomic efficiency.[29] The consensus seems to be that, with these "dynamic" developments, central planning theory has rid itself of its earlier static perspective.

2) *The Alternative Account of the Debate*

a) *pre-1920:* The standard view is not sufficiently cognizant of the extent to which the Marxian model of socialism was dominant—if not particularly explicit—in socialist economics before 1920. It is true that most socialists avoided any direct discussion of the workings of proposed socialist institutions, but a very definite idea of their conception of central planning is nonetheless evident from their critique of capitalism. Both the dismal failure of the attempt to abolish markets and money during the War Communism period in the USSR, and the arguments of Mises and Hayek, make this early idea of socialism very difficult to defend today. However, this largely rejected early vision of central planning is the most consistent and important of any that have been developed, and therefore its abandonment marks a far more serious retreat by socialists than the standard view suggests.

b) *Mises:* Mises was not denying the validity of the "pure logic of choice" for socialism; he was, on the contrary, insisting that central planners *must* find a way to apply this kind of logic to socialism or they will be doomed to calculational chaos and be unable to use resources efficiently. By our interpretation Mises was definitely *not* making an equilibrium argument and was aware that under static assumptions there is no problem for central planning. His discussion was primarily directed at proponents of Marxian socialism and was thus centered mainly on the argument that prices (and not some objective value measure such as labor hours) are necessary for rational calculation. However, contrary to the standard view, his argument is fully applicable to all forms of socialism which advocate common or state ownership of the means of production. Properly interpreted, this challenge has yet to be adequately answered by advocates of central planning.

c) *equation-solving:* Barone's argument is fully consistent with, but much less complete than, Mises' challenge. It simply establishes the formal similarity between socialism and capitalism under static conditions: if the number of (independent) equations equals the number of unknowns the system is "determinate". Mises maintained that such equations were inapplicable to the real world of continuous change even if, given a powerful enough computer, they were solvable.

d) *impracticability:* The central arguments advanced by Hayek and Robbins did not constitute a "retreat" from Mises, but rather a clarification directing the challenge to the later versions of central planning

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via "equation-solving" and "trial and error." Although comments by both Hayek and Robbins about computational difficulties of the equation-solving approach were responsible for misleading interpretations of their arguments, in fact their main contributions were fully consistent with Mises' challenge and were similarly unanswered.

e) trial and error: The "trial and error" response to the Austrians was based on a close analogy with the perfect competition model which itself does not explain dynamic price adjustment under realistic conditions of change. Thus, contrary to the standard view, Lange's model does not constitute an answer to the Misesian argument.

f) conclusion: The usual conclusion that economic theory cannot decide any important issues in comparative economics is valid only if "economic theory" is seen as strictly static equilibrium analysis. The broader Austrian conception of an economic theory that deals with change can shed considerable light on comparative economics issues and can help us to understand many of the practical problems of the mixed economies of both the East and the West. The Austrians did not limit discussion to the extreme "Isms," but explicitly contrasted mixed economy models with "pure" capitalism and socialism.

g) beyond the debate: The modern "planometric" and "macroplanning" attempts to advance central planning theory beyond the static framework of the early market-socialists have retained essentially static assumptions in their analyses.

Joseph Schumpeter

The interpretation of the calculation debate that has been offered by Joseph Schumpeter, deservedly considered among the greatest historians of thought in economics and one of the most influential contributors to comparative economics, will be an appropriate, authoritative starting point for our survey. Although he devoted only a few pages—in the "Equilibrium" chapter—of his monumental *History of Economic Analysis* to the issue, a great deal of his *Capitalism, Socialism and Democracy*[30] (especially chapter XVI) discusses the debate specifically. Schumpeter's account not only conforms with the standard view of the controversy, but it has also been extremely influential in the development of the consensus around this view.

Schumpeter sharply divides the debate into three separate questions concerning, respectively, the theoretical possibility, the practicability in principle, and the relative efficiency, of socialism from an economic point of view. He begins by asking "whether or not there is anything wrong with the pure logic of a socialist economy." It is clear from his discussion that he is referring to the question of the determinateness of a static equilibrium formulation for a socialist society. He poses the question whether the data and

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rules of rational behavior under socialism would still "yield equations which are independent, compatible—i.e., free from contradiction—and sufficient in number to determine uniquely the unknowns of the problem before the central board or ministry of production."[31]

His answer to this question is an unqualified yes. Indeed he registers some surprise that anyone could have ever denied it and that orthodox socialists failed to produce an answer to it until they were "taught their business" by bourgeois economists such as Pareto, Barone, and Wieser. At this time Schumpeter unambiguously describes Mises as "the only authority standing for denial that we need to mention," although in his later work he was to express some doubt about this interpretation.[32]

Schumpeter believes it to be clear that "economic rationality" can be attained without actual markets in capital resources and that "this follows from the elementary proposition that consumers, in evaluating ("demanding") consumers' goods, *ipso facto* also evaluate the means of production which enter into the production of those goods."[33] He formally derives demand functions for consumers goods and supply functions of labor and saving, and then confidently asserts that "the reader will have no great difficulty in seeing how, guided by these functions and by its own technological knowledge, the ministry will cause appropriate quantities of consumers' and investment goods to be produced."[34] The ministry can dispense with a capital market by "allocating productive resources—all of which are under its control—to...industrial managements according to certain rules": (1) they "must produce as economically as possible"; (2) the planning apparatus "declares itself ready to 'sell' to any industrial management unlimited quantities of producers' goods and services at stated 'prices' "; and (3) the managements assure that "production in all lines should be such as to make 'prices' equal (not merely proportional) to marginal costs."[35]

Under these conditions the task of each industrial board is "uniquely determined."

> Exactly as today every firm in a perfectly competitive industry knows what and how much to produce and how to produce it as soon as technical possibilities, reactions of consumers (their tastes and incomes) and prices of means of production are given, so the industrial managements in our socialist commonwealth would know what to produce, how to produce and what factor quantities to "buy" from the central board as soon as the consumers have revealed their "demands."[36]

Thus under socialism the mechanism for the realization of the equilibrium solution is the Central Planning Board (the CPB) rather than a market in capital goods. The ministry of production "has simply to set a single price on every kind and quality of producers' goods...and to see to it that that price exactly 'clears the market.' " On a purely theoretical level Schumpeter concludes that there are no grounds for doubting the "determinateness" or "formal rationality" of the socialist system.[37]

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Next Schumpeter endeavors to meet the "practical impossibility" argument to which he says Hayek and Robbins retired "after having accepted defeat on the purely logical issue." He believes he can "easily dispose" of this argument as well, which he dispatches with a cursory remark that "a glance at our solution of the theoretical problem will satisfy the reader that it is eminently operational." The ministry of planning, he asserts, "would command information sufficient to enable it to come at first throw fairly close to the correct quantities of output in the major lines of production, and the rest would be a matter of adjustments by informed trial and error." In fact Schumpeter, going further in this respect than the standard view generally does, agrees with Lange that the "market-socialist" solution to the Austrian challenge would not only be *as* possible but would be even "easier" than the capitalist one. In particular a whole class of "uncertainties" that plague capitalists concerning "the reaction of one's actual and potential competitors and about how general business situations are going to shape" can be expected to "vanish almost completely" under socialism.[38] The more standard view on this issue is that while socialism can eliminate some kinds of uncertainties relative to capitalism it may in practice aggravate other kinds.

Having established, at least to his own satisfaction, that socialism is both theoretically and practically possible, Schumpeter goes on to his third consideration: the relative efficiency of socialism as compared with capitalism. He holds that "pure theory contributes little to the solution of these problems"; it merely "helps us to posit them correctly and to narrow the range of justifiable difference of opinion."[39] He admits, as do most commentators on the debate, that this sort of formal demonstration does not, in itself, "mean very much."[40] Nonetheless he seems to believe an answer to this question of relative efficiency again follows trivially from his previous discussion: "we need only glance at the implications of our proof of the possibility and practicability of the socialist schema in order to realize that there is a strong case for believing in its superior economic efficiency."[41]

The bulk of Schumpeter's considerable analytical energies concerning these issues seems to have been expended on the first, purely theoretical equilibrium argument. His conviction that the second and third arguments follow directly from "glances" at the preceding discussion places perhaps a bit more weight on this first argument than it will sustain. But, in his disproportionate attention to the equilibrium argument he is fully within a tradition that has been consistently observed both by the market-socialist participants in the calculation debate and by most of its later historians.

The discussions on the debate in his later book (*History of Economic Analysis*) while still conforming in most respects to the standard view, retreated substantially from his earlier interpretation of Mises, as well as from the implication of this view, that Hayek and Robbins were arguing something substantially different. In one place he notes that "it is sometimes

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not easy to tell whether the...critics of the socialist plan, especially von Mises, really meant to deny the validity of the Pareto-Barone result." In another place, after establishing what he calls the "logical credentials of socialism," he refers in a footnote to another "purely theoretical" argument (not so designated in his earlier discussion), which he attributes to Mises as well as to Hayek and Robbins: "that, although there *exists* a determined set of solutions of the equations that describe the statics of a socialist commonwealth, there is, without private property in means of production, no mechanism by which to *realise* them." He pronounces this theoretical argument "definitely wrong" for the same reason he rejected the "practical impossibility" argument. The solutions to the Walrasian equations can be "realised" by "the method of trial and error."[42]

Although Schumpeter still considered the Austrians' theoretical critique of socialism to have been decisively met by Lange, it is significant that in his later discussion he was no longer willing to confidently attribute a purely static equilibrium argument to Mises, according to which interpretation Mises was refuted by earlier writers such as Barone. Unfortunately the standard history has continued to perpetuate Schumpeter's earlier assessment of Mises which we will argue is demonstrably incorrect.

Abram Bergson

Abram Bergson's essay, "Socialist Economics," has been by far the most commonly referenced secondary source on the calculation debate. Schumpeter was to say of this essay that its description of the development of the pure theory of socialism "leaves nothing to be desired,"[43] while Benjamin Ward was to refer to the socialist controversy as having "formally ended with Bergson's summary of the issues."[44]

Like the later Schumpeter, Bergson was unwilling to completely and uncritically adopt Lange's equilibrium interpretation of Mises' argument, but Bergson definitely leaned strongly toward that view. Concerning the questions raised by Mises "as to whether socialism can work at all, and how well," Bergson begins his article by pointing out: "By now it seems generally agreed that the argument on these questions advanced by Mises himself, at least according to one interpretation, is without much force."[45] He suggests that the later emphasis of critics of socialism on the question of the possible incompatibility of planning with political freedom "has the appearance of a tactical maneuver to bolster a cause which Mises' theories have been found inadequate to sustain."[46] Thus Bergson appears to accept both Lange's interpretation and refutation of Mises.

In a section entitled "The Ends," Bergson lays out some issues concerning "the formulation of a scale of values, on the basis of which the alternative uses of resources are to be evaluated." Among these are (1) the question of the extent to which either consumer sovereignty or the CPB should

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dictate the ends of social production, and (2) the controversy over whether individual preferences are fundamentally incommeasurable or can be meaningfully aggregated into a social welfare function which the CPB could work to optimize.[47] The first of these, though important for other reasons, is irrelevant to the calculation debate, since Mises' challenge, as he explicitly noted, applies whether the ultimate preferences are those of a single dictator or of a free consumers' goods market. Likewise, the second issue over interpersonal utility comparison, while undoubtedly an important matter for economic theory (about which Mises took a very definite position), is not crucial to the calculation argument. Even an economy possessed of "utilometers" enabling an accurate and meaningful cardinal measurement of everybody's preferences would still face the problem of imputing these final demands into the higher stages of production.

The next section of Bergson's article, significantly entitled "Optimum Conditions," begins to approach the calculation argument in the standard neoclassical manner.

> In accord with familiar theoretic procedure, technical knowledge and tastes are taken as given. . . . On this basis it is possible to derive from the given ends a series of conditions ("equations") which must be satisfied if the optimum allocation is to be achieved. The optimum conditions are sufficient in number to determine the amounts of each and every sort of goods and services allocated to each and every use (the "unknowns").[48]

Bergson thus presents the formal case for the determinateness of a socialist equilibrium, giving some indication that this comprises a rather abstract "theoretical" argument based on some unrealistic assumptions rather than any sort of proof of practicability.

> Thus, if the scale of values implied by the ends were known in complete detail (that is, if all the utility functions were known), and detailed information were available on techniques and on the stocks of resources on hand, it would be possible at least theoretically to solve this system of equations for the concrete values of all the unknowns.[49]

Bergson then goes on to summarize the subsequent neoclassical contributions to the debate which have been "concerned chiefly to formulate explicitly the optimum conditions. . . and to develop the analysis to deal with various complexities." As with Schumpeter we have a preoccupation with equilibrium analysis, the refinement of the "optimum conditions" such as that the marginal rate of substitution for each pair of consumers' goods must be the same for all households, that "factors must be combined in a technologically optimum manner," and that the "marginal value productivity of each factor must be the same in every industry."[50] A considerable literature in welfare economics—to which Bergson had made a seminal contribution—has exhaustively studied these equilibrium conditions and has

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undoubtedly promoted clarity in our formal depictions of both capitalist and socialist equilibria.[51] The question remains, however, how producers would know what the "technologically optimum manner" of production or the "marginal value productivity of each factor" is, without a competitive capital market. Assuming technology to be "given" may be a legitimate analytical procedure within an equilibrium framework, but it crucially begs the whole question of the calculation debate.

In his section IV Bergson specifically addresses the issue of the contributions this abstract equilibrium analysis can make to the central planners' task. First, this framework might "assist the Board to formulate a conceptually satisfactory scale of values to guide the economy, one that is internally consistent and in principle at least covers the bill." Secondly, the analysis "establishes the implications of the given ends," i.e., the optimum conditions, which would be a "prerequisite for the construction of a planning scheme which might approximate the given ends in practice." It could be said that Mises' whole argument was essentially that, in practice, noncompeting producers could not determine the complex implications of the consumer demands with respect to the more efficient applications of the means of production toward those ends. But Bergson, at least in this article, seems to grossly oversimplify the practical difficulties involved in this imputation process.

> It happens that the criteria for the optimum that have been set forth are conceptually simple and, for the cases where small adjustments are possible, require for their application only facts which actually might be experienced in a given situation (the marginal rates of substitution, marginal productivities, etc.).[52]

Would such "facts" as marginal productivities really be "experienced" without a competitive process? Surely we cannot simply assume that actual market participants would have all the knowledge necessary for the economist's formal proof of a determinate equilibrium. That theoretical proof proceeds as if each producer initially had a complete "cookbook" of technological recipes which, in conjunction with the appropriate prices given to him by the CPB (or the Walrasian auctioneer), he uses in order to select his optimum production technique. Such a discussion may be helpful as an heuristic device in showing the interdependence of decisions in the market, but as a purported description of the decision-making process of actual producers this approach is very ill-suited and misleading.

When Bergson comments that the CPB would "adjust prices and wages from time to time in order to bring the demand and supply of goods and services into line,"[53] he seems to seriously underestimate the degree to which unexpected changes permeate a modern economic system. The economy appears as if it is normally in a state of equilibrium from which it is only occasionally disturbed. But, as Hayek and Mises were frequently to emphasize,

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the implications of an economy's being in equilibrium show that this is a totally unrealizable situation, in which, despite the passage of time, every agent's plans are perfectly meshed with everyone else's, in which genuine uncertainty has been banished, and in which such institutions as money and even prices would be superfluous. In such a world Lange's proposed "trial and error" solution would indeed be workable, since the CPB would have ample time to alter one "price," holding the others at their equilibrium values until complete equilibrium is reached.[54] As Hayek puts it, "With given and constant data such a state of equilibrium could indeed be approached by the method of trial and error. But this is far from being the situation in the real world, where constant change is the rule."[55]

Bergson in fact had serious doubts about the workability of Lange's solution in a continually changing world. He cited Soviet experience as indicating

> that on account of the economic as well as political problems there might be very real difficulties in the way of applying the trial and error Competitive Solution. Consider the matter of high-tempo industrialization, and the rapid shifts in demand and production schedules that would be associated with this process. In such a situation, the errors involved in the operation of the Competitive Solution might well be formidable; and evidently experience could not be very helpful in rectifying them.[56]

The Austrians in the debate, however, would contend that the "shifts in demand and production schedules" that occur in *normal* conditions, not just during "high-tempo industrialization," would be rapid enough to make the planners' task of locating a set of equilibrium prices by trial and error quite unmanageable. As he was to point out in a later essay, Bergson ultimately did not accept Lange's opinion that under the "competitive solution" convergence to equilibrium would be rapid, and he was to belatedly agree with Hayek that

> on the contrary the task of fixing prices for an entire economy, which Lange assigns to the Board, would prove formidable. Almost inevitably, the Board would find it difficult to respond quickly to continually occurring changes in supply and demand. It would also be unable to fix prices in sufficient detail to take into account almost endlessly diverse varieties of goods produced by a modern economy. Imbalances between supply and demand, therefore, might be large and persistent.[57]

Although this more recent assessment of the debate substantially agrees with the Austrians, Bergson's earlier and more influential discussion reflects a common neoclassical view of equilibrium as a normal situation of quantitative balance between supply and demand. By contrast Austrian economists view equilibrium as an entirely imaginary condition of complete coordination of plans where all "changes" are fully anticipated. As such, it may

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be a useful, even an indispensable, tool of analysis, but according to the Austrian view it is never attained in any real economy. The fact of continuous disequilibrating change renders a "trial and error" process of equilibration unworkable since we could never know which of many prices are at disequilibrium with respect to some actors' plans at any time. As Mises later remarked in this regard, "The method of trial and error is applicable in all cases in which the correct solution is recognizable as such by unmistakable marks not dependent on the method of trial and error itself."[58]

To his credit, Bergson in 1948 did acknowledge that in practice the CPB may encounter some severe difficulties in administering Lange's system. Among these he specifically cites three: (1) the fact that "the vast stock of detailed knowledge" necessary would be "scattered throughout the community" and the amount of this knowledge available would itself "depend on the particular administrative procedure used"; (2) it would be "physically impossible" for the Board to decide successively on all the myriads of possible alternatives; and (3) it would be difficult to control the execution of the plan once it had been formulated. [59] Each of these points was specifically argued in the debate by Hayek and will be examined here later in more detail. Bergson seems to have believed in 1948 that the so-called "competitive solution" offered by Lange, Taylor and Dickinson (particularly in Lange's "very systematic exposition") by and large overcomes all of these potential difficulties. Bergson points out the relevance to the debate of Hayek's later contributions about "The Use of Knowledge in Society," and his description of the kind of "detailed knowledge of time and place" which "by its nature cannot enter into statistics" and "cannot be conveyed to any central authority in statistical form."[60] Bergson finds these remarks a "wholesome antidote" to the tendency of many socialists to view the ministry of planning as a "committee of Supermen." However, he does not accept Hayek's conclusion that these necessary limitations on the knowledge of the CPB would render the task of setting prices impracticable, since he believes that this task can be decentralized, i.e. "broken down functionally and geographically," and be guided by "general directives" issued by the CPB.[61] He also dismisses Hayek's contention that the CPB would have to continually conduct detailed audits of the cost records of the individual firms, which if true would seriously impair the decentralization advantages intended in the "competitive solution." Bergson proposes that by tying managerial incentives to profits and comparing profits of different firms the Board could dispense with such detailed studies.[62]

Underlying this particular controversy is an ambiguity concerning the extent to which the "competitive solution" actually introduces competition into the economy. We would contend that, if genuine rivalrous competition and the market equilibrating process are *not* fully permitted in the "competitive solution", the planners will not be able to escape Hayek's problem of "scattered knowledge" as easily as Bergson suggests. If, on the other hand,

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such full-fledged competition *is* allowed, the resulting system will be indistinguishable from private ownership of the means of production.

A less conciliatory attempt to answer the calculation challenge has been the "Centralist Scheme" favored by Maurice Dobb. Bergson points out how this approach would seem to bring back the problem of "solving millions of equations" which the "competitive solution" was designed to resolve. Such difficulties could be reduced, however, if one can assume fixed coefficients of production under which, in effect, relative prices can be ignored, and under which there is no basis for speaking of the marginal productivity of any one factor. Bergson notes that "Leontief found it practicable" in his famous input-output study of the American economy "to assume that for broad industrial groups the production coefficients are constant."[63] If fixed coefficients could be assumed, the planners would only need to devise technologically feasible allocations of resources rather than economically efficient ones. But we would contend that both the level of aggregation and the span of time for which input-output applications have been used are far too broad to aid the microeconomic production decisions with which the calculation debate was concerned.[64]

Finally, at the end of the article, Bergson returns to the question he had raised at the beginning: what Mises meant when he asserted the impossibility of economic calculation under socialism. Unlike many treatments of this point, he at least admits there are two possible interpretations of Mises, those of Lange and Schumpeter on the one hand, and that of Hayek on the other.

Before describing these interpretations Bergson offers to "let Mises speak for himself" and selects four quotations[65] from Mises' essay on "Economic Calculation in the Socialist Commonwealth," which rather forcefully make the point about the necessary relationship between private ownership and prices, and between prices and rational economic calculation. Largely because of their forceful style of expression these quotations could be seen as consistent with Lange's interpretation of Mises, but in actual content they are consistent with either interpretation. Unfortunately Bergson did not choose to select the following quotations from the same group of pages which strongly support Hayek's and explicitly contradict Lange's interpretation:

> The static state can dispense with economic calculation. . . . But this is only conceptually possible. . . . a static state is impossible in real life, as our economic data are forever changing, so that the static nature of economic activity is only a theoretical assumption corresponding to no real state of affairs, however necessary it may be for our thinking and for the perfection of our knowledge of economics.[66]

As was argued earlier, no statement in economics stands alone. To be rendered fully intelligible it must be examined in terms of the wider conceptual framework from which it stems. It is not enough to select a few quotes,

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"read innocently," to prove what Mises meant, for these words must be given meaning by relating them to the system of thought of the reader. For Lange, Schumpeter, and Bergson, rational economic calculation means calculation with equilibrium prices, but not for Mises.

Of the two interpretations Bergson considers, the one "which seems to have gained the wider currency" is Lange's: that rational calculation is "ruled out conceptually" even for a "Board of Supermen, with unlimited logical faculties, with a complete scale of values for the different consumers' goods and present and future consumption, and detailed knowledge of production techniques." If such an argument has ever been maintained by anybody, it would, as Bergson said, certainly be "easily disposed of" and would have already been

> refuted completely by the work of Pareto and Barone. As the analysis of these writers shows, once tastes and techniques are given, the values of the means of production can be determined unambiguously by imputation without the intervention of a market process. The Board of Supermen could decide readily how to allocate resources so as to assure the optimum welfare. It would simply have to solve the equations of Pareto and Barone.[67]

It would be difficult to reconcile this interpretation of Mises with his specific reaction to Dickinson's similar "superman" assumption: "We do not deal with the acts of the omnipresent and omniscient Deity, but with the actions of men endowed with a human mind only. Such a mind cannot plan without economic calculation."[68]

Fortunately there is another interpretation of Mises, the one given by Hayek, that "Imputation is theoretically possible; but, once private ownership of the means of production has been liquidated, it cannot be accomplished in practice."[69] This, too, Bergson says, can be interpreted in two ways (represented in Schumpeter's second and third questions above), "whether a planning scheme can be devised such that it can work at all" or "which is more efficient, socialism or capitalism." Concerning the former interpretation of "impracticability," Bergson is convinced that both Lange's trial and error argument and even the simple existence of the Soviet Union refute that claim. The latter issue of relative efficiency between capitalism and socialism, then, "is now the only issue outstanding."[70]

Yet in fact this last question was *always* the only issue outstanding and all the involved discussions of "conceptual" possibility and practicability "in principle" have only diverted the debate from its original and essential content.[71] Mises, Hayek and Robbins never denied that socialism would be "possible" under static conditions, though they had serious doubts about the possibility of those conditions. They were denying that any procedure could be found which was efficient enough at impelling an equilibrating process to supplant the function of the capitalist-entrepreneur under private ownership of the means of production.

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In 1948 Bergson viewed Hayek's arguments concerning the unworkability of Lange's solution as generally unsuccessful and this assessment has been preserved in many subsequent accounts of the debate. But just as Schumpeter reversed himself in his interpretation of Mises, Bergson was to change his mind substantively about Hayek, and in both cases it was the earlier—and in our view the less defendable—version that has been more influential in the history of thought.

In his later article, "Market Socialism Revisited,"[72] Bergson argues, for example, that the "failure" on the part of Lange and his school "to establish any practical success criterion for managers" now seems to be a more serious deficiency than he had thought before, when he had said "our impression is that the question of managerial incentives would not present any serious difficulties." While earlier he had concluded that "there is no reason to suppose" that managers under public ownership "would necessarily be too venturesome or, as Hayek argues, too cautious,"[73] his later opinion had substantially changed.

> Given a satisfactory test of success, managerial incentives must still be related to it appropriately. Hayek argued that such a result might not be easy to achieve. In practice, managers very likely would be reluctant to take risks. This is perhaps not inevitable, but the construction of a satisfactory incentive system now appears more difficult than I envisaged it to be previously.[74]

Invariably the process by which an original controversy is summarized in secondary sources and digested by later thinkers until it filters its way into the textbooks is a gradual one. It was unavoidable that some of the earliest discussions of the calculation debate—of which Schumpeter's and Bergson's were the most often cited—would have had a greater impact than any more recent second-thoughts are apt to have had. Many third-level accounts of the debate were written before Schumpeter and Bergson changed their minds about Mises and Hayek, while fourth-level discussions in contemporary textbooks have often relied on these third-level discussions. Thus the standard version of the debate still retains errors—or so they are considered by this reader—which the authors themselves have long since corrected.

Benjamin Ward

Neither the Austrian nor the neoclassical paradigm has stood still in the intervening years since they clashed in this controversy in the 1930's. Benjamin Ward stands out as one of the leading contemporary neoclassical historians of the debate and not only his own account of the original arguments but also his view of how the subsequent developments in neoclassical theory relate to those arguments will be briefly examined. In addition we will contend that the modern Austrian developments in critique of neoclassical

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economics parallel in many ways the original Austrian differences with the neoclassical market-socialists of the debate.

Ward's most systematic treatment of the comparative economics topics surrounding the debate is his influential book *The Socialist Economy: A Study of Organizational Alternatives* (1967),[75] the stated aim of which is "to relate aspects of socialist organization to economic behavior." Ward explicitly used "the socialist controversy" we are examining as the "paradigm for establishing such relations,"[76] and his detailed discussion and critique of the debate in Chapter Two comprises the basic conceptual framework for his whole book.

For Ward, the "heart" of the socialist controversy is the question: "Can a socialist society find some method of organizing the allocation of resources which will permit the economy to function with a tolerable degree of efficiency?"[77] After some sixty years of debate, he notes that "many, perhaps most, economists would consider it established that the appropriate answer is 'yes.'" Ward argues that the question as posed should, however, be considered still open, since there is a "variety of conceivable forms of socialist economy" and the answer "may not be 'yes' for every one of these."[78] Yet despite his more balanced conclusion, Ward's analytical account of the controversy fits the standard version in most respects rather well.

He begins his survey of the debate with a general statement of the crude condition of socialist economics before Barone. An attitude of mistrust of marginalist economics and almost exclusive attention to condemnations of capitalism were combined with a "rather utopian view of life under socialism" which sometimes seemed to specifically deny that scarcity would be a problem under socialism. Ward refers to Wieser's *Natural Value* as an important early contribution which showed that "the problem of scarcity and the problem of relative valuation of alternatives derivative from it were equally problems of capitalism and socialism."[79]

However, Ward attributes the "first application to the socialist problem of the formal general equilibrium analysis developed by Walras and Pareto" to Barone's "Ministry of Production."[80] In this "significant step forward" Barone "attempts to show that the form of the imputation rules for a socialist and capitalist society are the same."[81] Ward credits Barone with having demonstrated "in a more explicit way than had been done previously, that prices are not conceptually bound to the market."[82] Barone offered hints of both the "equation-solving" and "trial and error" methods of attaining equilibrium prices that were to resurface in the later controversy though he did not appear very optimistic about their workability in practice.

Ward then speaks of a "retrogressive diversion" of the debate around 1920 that reverted to debating "the possibility of establishing a 'natural' socialist economy, or one in which money and pricing are completely absent." He lists Otto Neurath and Nicolai Bukharin as proponents of this step back-

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wards to the view "that prices were inevitably tied to markets and capitalist exploitation" and suggests that "Mises may well have had the natural economy in mind when he asserted that socialism was 'impossible.'"[83]

This interpretation of the early confrontation between Mises and Marxism is misleading in two important respects. First, to speak of the anti-market attitude of two Marxists as a "retrogressive" development is to implicitly credit Barone with far more influence than he actually had at the time, and to considerably understate the degree of acceptance of the Marxian view that socialist planning could and must dispense entirely with prices. According to Ward's account this model of socialism was but a temporary aberration in 1920, while we would argue that it was widespread before 1920 and is firmly rooted theoretically in Marx and Engels.

Secondly, this account leaves the misleading implication that Mises' argument applies only to this extreme notion of central planning. Although it is valuable to recall that Mises was *directing* his argument at this, the predominant version of socialism of his time, rather than at the market-socialist systems that emerged only later and in response to his challenge, it does not follow that the logic of his argument applies only to this largely abandoned program. The challenge would, to be sure, have to be reformulated with market-socialism in mind, as was done by Hayek,[84] but substantially the same problem of rational economic calculation would have to be faced by any system in which there was common or state ownership of the means of production.[85]

Ward's account of the debate proceeds with a fairly sympathetic discussion of Taylor's and Lange's argument that the difficulty of rational economic calculation could be overcome "by applying the same rules for adjustment to socialist factories as Walrasian economists attributed to competitive capitalist ones." This, we are told, would be "a relatively simple job for the Ministry" and would be no more difficult for socialist firms than economic calculation already is for capitalist firms.[86] We contend that this "trial and error" solution is neither as similar to real capitalist price adjustment nor as trivial an analytic matter for a world of continuous change as Ward seems to believe.

The next section of Ward's survey, interestingly entitled "Hayek and Dobb," notes briefly some objections raised against market-socialism from these two very different perspectives. In spite of the obvious disparity of viewpoints, Dobb and Hayek appear to have been making somewhat similar accusations against neoclassical market-socialism when they focus respectively on "dynamic problems associated with market adjustment" and "the role of information in resource allocation."[87] A crucial assumption of the perfect competition model upon which market-socialism was constructed is that there is full coordination between the supposedly separate decentralized decision-makers; that there is no true uncertainty[88] either with respect to the developing environment in which each chooser finds himself or with

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respect to the choices of others that are simultaneously being made. The vital and difficult questions of information flow (of learning) are obscured in an equilibrium framework which simply takes "tastes" and "technology" as data somehow already given to every firm. The real world, however, is replete with ignorance of these supposed "givens," as both these critics emphasize.

Maurice Dobb, favoring a more centralized model of socialism, locates the source of this ignorance in the decentralized organizational form of a market society with private ownership of the means of production. Ward's summary of Dobb's position stresses what contemporary Austrians call the "simultaneity problem"—that different and uncoordinated production decisions that conflict with one another are made simultaneously under capitalism—as well as the argument that expectation formation under capitalism is inherently irrational.[89]

> Expectations are contagious... and small individual producers are unaware of what is going on elsewhere at the time they make key production and investment decisions. Dobb feels that the time lag between the making of decisions and the collection of the relevant information, plus bandwagon effects, accounts for much of the fluctuation of price and output in markets, a fluctuation which is wasteful and which would not be avoided under market socialism.[90]

Hayek, on the other hand, favoring private ownership of the means of production, would locate the source of this ignorance more fundamentally in the limitations of the human mind rather than in the market form of social production. Once it is understood that in the light of Mises' argument it would be impossible for all decision-making to be subsumed under a unitary central plan, we have no alternative but to permit separate simultaneous decision-making by decentralized segments of society. Hayek would agree that a degree of discoordination of these separate plans is, as Dobb argues, "an inevitable consequence of market organization," and that as a result the market economy is continuously in disequilibrium. He might even agree that, viewed from an ideal equilibrium perspective, this discoordination could be called "wasteful," but he would insist that it is not the proper method of comparison, as Schumpeter always stressed, to contrast an actual imperfect world with an hypothesized ideal one. The point of the calculation argument was not that a market *is* in equilibrium while a socialist economy is not, it is that a market possesses an equilibrating process which tends to coordinate the separate agents, while a socialist economy would lack this coordinating process.[91]

Ward credits Hayek with having "added... two important new issues"—the role of information and of risk-taking—to the socialist controversy,[92] though Hayek himself seemed to believe he was only elaborating these points from discussions by Mises.[93] It is true, however, that especially in his

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subsequent contributions on knowledge, Hayek was to add significantly to our understanding of the limitations of equilibrium theorizing. As Ward acknowledges, "In contemporary economics the starting point for the discussion of information is Hayek's work, and its significance appears to have first occurred to him while studying the socialist controversy."[94] Although Ward seems to concede that the difficulties of gathering the scattered knowledge necessary for economic decision-making would be telling against a fully centralized model, he finds the approach of Taylor and Lange to be immune from this criticism. Explaining in a footnote that at the time (1935) Hayek had only "some word-of-mouth knowledge of market-socialism" and "does not appear to have been familiar with Taylor's article," Ward[95] claims that Hayek "does not seem to understand how the Taylor adjustment rules might be used in practice." Ward interprets the market-socialists as advocating the genuine decentralization of production decisions and thus concludes that Hayek's overly pessimistic estimate of the difficulty of "centralized" planning "is based on the assumption that the plan must be made in some central agency."[96]

Indeed such an assumption was the initial view of most adherents as well as critics of central planning, but Hayek was to deal specifically with the market-socialist attempt to partially decentralize planning. It is curious that of Hayek's two essays which discuss market-socialism[97] Ward refers only to the earlier one, written as he says before Hayek had seen the full Lange-Taylor model. His later essay, which dealt extensively with Lange's and Dickinson's proposals, is nowhere mentioned in Ward's book. As Hayek explained in this essay, the problem with the so-called "competitive solution" is that it presumes that socialist managers will obediently employ society's resources in accordance with the rules handed down to them from the ministry of production. The attitudes of such rule-following bureaucrats to the resources under their control would necessarily differ from those of private and competing owners who undertake projects at their own initiative, at their own risk, and for their own profit. It would therefore be necessary to somehow monitor plant managers' performance and this would itself require the very centralization of information the market-socialists were trying to avoid. Yet, Hayek argues, if fully self-motivated action is to be permitted to market-socialist plant managers (if they are to be free to take their own risks, reap their own gains, and offer competing bids for resources), this would entail that they be private owners of the means of production, thus abandoning the last vestige of socialism. The market-socialists were conveniently ambiguous about the degree of decentalization they were proposing, but Hayek specifically addressed a large variety of alternative proposals in his 1940 article.

Ward's survey of the socialist controversy is completed with a discussion of Abba Lerner's *Economics of Control*, a book which is infused through-

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out with this market-socialist ambiguity. Lerner wishes to preserve the market mechanism and even "socially productive speculation"[98] while retaining a controlled rather than "haphazard"[99] organization of production. The confusion over these incompatible goals arises from the tendency of neoclassical theorists to think exclusively in equilibrium terms.

Lerner's overall argument, Ward says, is "a good one, that is, it 'solves' the problem of distribution within the context of the classical static economic analysis by describing equilibrium properties," although the "manner in which price adjustment would occur in the Lernerian system is quite unclear."[100] But, as we have been arguing, it is precisely this largely ignored matter of price adjustment, not static equilibrium, that is the point at issue in the debate. Lerner deliberately restricted his analysis to what he called a "theoretical" solution,[101] that is, to the "static state" which Mises and Hayek had admitted from the very beginning of the controversy would face no problem of economic calculation. Clearly if advocates and opponents of socialism are to confront each other directly in useful debate, the analysis will have to be carried beyond this equilibrium framework within which all participants seem to agree there is no problem. The most serious shortcoming of Ward's discussion of the debate is that he attributes this preoccupation with static equilibrium to the controversy as a whole rather than, as we would argue, to its market-socialist participants.[102]

Ward recognizes that this exclusive focus on static equilibrium severely limited the results of the classic controversy—"there appear to be no clear-cut answers about the feasibility of the socialist form of economic organization"—and attributes this to the insufficient development of economic analysis at the time. In a section entitled "The Present State of the Debate" he endeavors to fill in the "gaps and failures" of the original discussion "from the point of view of contemporary economics."[103] He refers in this respect to some refinements of general equilibrium analysis[104] and to extensions of this formal approach to studies of "the stability and convergence properties of general equilibrium models"[105] and "nontâtonnement processes."[106]

However, the fundamental flaws of the original controversy are rooted in a neoclassical perspective that has been retained in these modern contributions. The basic conception of choice that underlies these contributions is still the narrow "optimizing" notion that had pertained to pure equilibrium analysis. It is significant that the primary emphasis of the modern Austrian school that stems from Mises and Hayek is on precisely the narrow nature of neoclassical choice theory even in its supposedly non-static forms today.

The original market-socialist participants in the debate believed that they were advancing beyond pure equilibrium analysis when they postulated that the ministry would adjust prices by "trial and error" until the equilibrium was "found," much as neoclassical theory conceives the Walrasian auctioneer doing in a market economy. But the Walrasian approach itself does

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not explain price adjustment, so it scarcely serves as an argument for the feasibility of market-socialism to suggest an analogy with this approach. This model cannot explain the movement of prices since everyone is supposed to passively take prices as "parametric." It therefore has to employ the fiction of a centralized auctioneer as its *Deus ex machina*.

Perhaps the most crucial difference between this imaginary auctioneer adjustment model and the real world concerns the question of trading at "false prices." Contrary to the assumptions of the Walrasian approach, in actual market exchanges there is no way to prevent the data from changing before an equilibrium constellation of prices can be found. As Edgeworth pointed out, this means that trading in the market will invariably take place at disequilibrium prices, and this is itself a disequilibrating force.[107]

Yet many of the same theorists who explicitly recognize that the auctioneer model is unlike real market processes nonetheless endeavor to model central planning schemes after the Walrasian procedure. Indeed many advocates of "planometrics," iterative computational techniques for adjusting prices to equilibrium, insist that it is a strength of their approach that they can, by using an auctioneer-like approach, attain equilibrium "more easily" than real markets can with their problems of "false trading." Thus Ward, in his contrast between centralized and decentralized models of socialism, seems to consider it an advantage of centralized models that "no goods would be traded until the adjustment process, carried out by paper and pencil, or rather computer, had arrived at the optimal plan for quantities and prices,"[108] whereas decentralized models have to contend with the "problem" of allowing irreversible exchanges to take place at disequilibrium prices.

We would contend that this is a peculiar way of looking at the issue of trading at "false prices." Actually such trading, though perhaps a liability for formal general equilibrium analysis, is a definite advantage of real market processes over planometric models. The fact that the latter have never proved practicable can largely be explained by their lack of this "problem" of disequilibrium transactions. The chief strength of the real equilibrating process, as contrasted with auctioneer-type models, is that it works tolerably well *without* eliminating exchanges at "false prices," and, in particular, by taking advantage of knowledge actively being generated by the disequilibrium competitive process.

Ward discusses a number of planometric models, concentrating on some linear programming methods proposed by Montias, Malinvaud and Dantzig,[109] all of which require that trading and production cease while supply and demand information throughout the structure of production is communicated to the ministry of production. The advantage of these schemes is supposed to be that the technological knowledge (the coefficients of production) need not be known by the central planners, this feature alleg-

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edly insulating them from Hayek's critique. Each of these procedures requires that an iterative process of searching out the equilibrium be performed and results communicated back and forth between plant managers and the CPB. In every iteration the producer is supposed to examine a provisional constellation of prices and react to it with a new set of optimal demands of inputs and estimates of outputs that he can expect to deliver if these prices are decided upon. The CPB then performs another computation with this information and produces a new set of prices. This procedure continues until equilibrium prices, or an acceptable approximation thereof, are established. Then and only then, production and trading can be renewed.

Aside from the practical difficulties of implementing any of these models,[110] their fundamental problem is that they, like the Walrasian approaches from which they stem, trivialize the problem of the dispersion and acquisition of knowledge in the production process. Each producer is assumed to already have at his disposal a complete set of technologically feasible production methods into which he need only plug the CPB's computed prices in order to decide the best combinations of resources. We would argue on the contrary that producers discover feasible and more efficient methods of production only by *trying* different ones and either failing or succeeding, success being revealed only in profit and loss figures. The advantage of the nontâtonnement equilibrating process is that it depends on the competition of separate private owners who disagree about which techniques are better. This competition permits different entrepreneurs to try their hand at proving their views on the market by making a profit. Those with more accurate expectations and more efficient technological methods struggle rivalrously against those with less. Market competition is thus what Hayek calls a "discovery procedure" in which the extensive knowledge which neoclassical economists graphically depict in simplistic production possibility surfaces, is not, in fact, inherently in the mind of the plant manager any more than it could be at the disposal of the CPB. Without an ongoing competitive discovery process the manager, too, would be ignorant about what methods are more efficient than others.

Hayek's discussion of the difficulties of centralizing the dispersed knowledge of an economy has frequently been interpreted, by Ward as well as other modern theorists, as indicating only that the producer's choice of the optimal production technique must be decentralized, while the adjustment of prices could still be performed by a central bureau equipped with a sufficiently powerful computer. We will contend, however, that this dichotomy between the discovery of correct prices and the discovery of efficient production techniques is an artificial theoretical procedure that begs the essential questions of the calculation debate. In the real-world market process, "trial and error" experimentation with techniques and prices are in-

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extricably bound together. Actual producers simultaneously bid prices up and down as part of their experiments with production techniques and without this competitive process would not know what techniques are better.

Others: Lippincott, A. Sweezy, Dobb, Knight

Benjamin E. Lippincott. In his introduction to the influential 1938 book that contains Taylor's and Lange's central contributions to the debate, Lippincott repeats virtually every detail of Lange's interpretation of the calculation argument. We are told that Mises' argument "had really been disproved early in the century by Barone," who "proved that in principle the accounting prices of a socialist economy would be as economically significant as the market prices of a competitive economy." Lippincott further believes that this "mathematical demonstration using simultaneous equations" is sufficient to "demonstrate that it was possible for a socialist economy to make a rational allocation of resources." Like the other neoclassical interpreters of the debate, he emphasizes "the great formal similarity of a socialist regime to a competitive one" purely on the abstract equilibrium level of analysis, and from this (admitted) similarity he immediately concludes with an assertion that socialism is "theoretically" possible.[111] And, as with most neoclassical treatments of this issue, he trivializes the complex process of imputation when he states that "it naturally follows...that the preferences of consumers, as expressed by their demand prices...are the guiding criteria of production, and ultimately of the allocation of resources."[112]

We have argued that this prevalent Lange-Schumpeter interpretation of Mises—that he was denying that there could be defined a determinate equilibrium under socialism—is mistaken, and in particular that it fails to take into account the essential differences between the Austrian and neoclassical paradigms. Lippincott goes even further by explicitly identifying the Austrians as merely a branch of a rather broadly defined "orthodox" economics, by which he means "economists of the school of Marshall and of the Austrian and Lausanne schools." All three branches of marginalism are indicted together for dealing exclusively with static analysis:[113]

> Holding that the proper field of economic theory is the field of pure abstraction, where logic and mathematics can be rigorously applied, they have limited their analysis very largely to a condition of static equilibrium—a condition where change is ruled out and economic forces are in balance. As a result of this, they have given little attention to institutional considerations.[114]

Although early Austrian economists must share some of the blame for expressing their arguments in such a way as to permit this association with neoclassical equilibrium theorizing, they were never primarily concerned

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with equilibrium and were quite seriously interested in "institutional considerations." The focus on static equilibrium has been much greater on the part of those who attempted to answer Mises and Hayek, while, contrary to Lippincott's suggestion, institutions have been of vital importance to Austrian theory since its inception with Menger's writings. That such theorists can be accused of stressing static equilibrium at the expense of institutions is a testament to the complexity of economic argumentation and the extent to which statements in our science—when not carefully related to the fundamental paradigm from which they were conceived—can be totally misunderstood.[115]

What is even more mysterious in Lippincott's case is that he goes on to argue that these criticisms of "orthodox" economics do not apply to all orthodox economists, and then cites as "exceptions" precisely the theorists who did in fact focus primarily on equilibrium in their economic analysis: Pareto, Barone, Taylor, Knight, and Pigou.[116]

Lippincott repeats Lange's statement that Hayek and Robbins were retreating from Mises' theoretical argument to a mere denial that socialism can work in practice, stressing as usual their comments about solving numerous simultaneous equations.[117] He considers the trial and error solution of Taylor and Lange to provide a conclusive demonstration that "the process of price determination in a socialist economy is quite like that in a competitive one."[118] We contend, on the other hand, that while this trial and error method of adjusting prices may bear great similarity to the neoclassical auctioneer adjustment process, it has little to do with the way prices are determined in competitive markets. Yet Lippincott asserts that, with this demonstration of the formal similarity of market-socialism to the Walrasian model, "the burden of proof has been shifted to the capitalist economy, which must now show why it should not be replaced by a socialist one, in view of its evident feasibility and superiority."[119]

We would contend that an elaborate description of the equilibrium conditions for socialism supplemented by a few remarks about adjusting prices by trial and error until this equilibrium is found does not constitute a case for the "evident feasibility" of socialist institutions in the real disequilibrium world, much less their superiority.

Alan R. Sweezy. Sweezy's 1936 essay on the debate represents one of the most explicit early statements of the standard account we have been describing. The Mises-Hayek argument "that socialist pricing would of necessity be purely arbitrary and hence meaningless," he says, "has been refuted in a way that should be definitive for informed students of economics by Dr. Lange."[120] Once again we find that the argument Lange is seen to be refuting has been first distorted by being translated into neoclassical terms. Sweezy asserts that in his book *Collectivist Economic Planning* Hayek "stages a battle between the mythical knight of a purely competitive capital-

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ism, in which everything works out for the best by definition, and the straw dragon of a patently unworkable type of planned economy. One is scarcely surprised to find that the knight wins."[121]

Sweezy suggests here both that Hayek's critique of socialism was formulated in terms of the perfect competition model and that it was directed at a straw man construction of socialism that lacks money and prices. Neither suggestion is accurate. It was no less a socialist than Karl Marx, hardly a straw man, who viewed socialism as logically requiring the abolition of money and prices, and it was the *responses* to Hayek and Mises that were framed in terms of the "mythical knight of purely competitive capitalism." Hayek was, himself, highly critical of these responses precisely on the grounds that this model is inadequate as a description of real-world capitalism.

In fact it is economists such as Sweezy who pay an inordinate amount of attention to the equilibrium state, and in particular to the perfect knowledge assumptions that underlie it, rather than to workable economic processes.

> All economists would agree...that when new productive capacity is being planned it should be extended to the point where the output thus provided for can be sold at a price just sufficient to cover the cost of producing that output, the best known organization of the factors of production being assumed.[122]

This last assumption begs the whole question of the calculation argument which asks whether the best organization of factors of production *can* in fact be known without the operation of a competitive process in the capital markets. Sweezy acknowledges that putting such economic formulae to work in practice would pose some difficulties, at least at first, but seems to have an inflated view of the practicability of the market-socialist model when he concludes that

> even with their present knowledge and analytical equipment, economists and production managers could formulate price-output policies which would be more in the social interest than those adopted by enterprises in the capitalist world.[123]

As Hayek pointed out, the matter of applying formal equilibrium theory to economics is being "treated as if the cost curves were objectively given facts." In actual markets any tendency to adopt minimum costs is only due to a continuous competitive discovery process.[124] An indispensable aspect of this process is that different owners with divergent knowledge and expectations concerning production methods contend with each other in a rivalrous market, struggling to outbid one another for the use of scarce resources. This discovery process is thoroughly absent from equilibrium constructions and from "trial and error" price adjustment methods. Sweezy writes:

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> There would be [under socialism] no exchange of ownership in the market for means of production. But as an accounting device it would be necessary to register the demands for and supplies of all commodities at their going prices and to compare these supplies and demands as a check on the correctness of existing price and output schedules.[125]

The crucial question is whether this planning technique of "registering" demands and supplies while centrally adjusting prices can be substituted for competitive bidding by private owners. Will the non-owners who cooperatively attempt to implement the central plan in accordance with Lange's rules have the requisite knowledge to express rational demands of the various factors of production if they are not actively contending with one another for these factors? Such questions are necessarily avoided under the knowledge assumptions of the neoclassical model.

Alan Sweezy does however offer some interesting insights on the important problem of uncertainty with respect to central planning theory. He points out: "In a completely stationary economy. . . there would be by definition no problem of planning," and, if we assume perfect foresight or instantaneous and perfectly fluid adaptation to change, there would be no substantial problem of planning. Such unrealistic models, he says, are "of little use in a discussion of socialism, which must take as its point of departure the economic world as it actually is.[126]

Exactly, but Sweezy does not seem to understand the extent to which the introduction of these more realistic assumptions undermines the market-socialists' "refutation" of Mises. We can agree that "in actual practice the task of organizing knowledge and coordinating policies in an advanced industrial economy is bound to be so stupendous that success can never be more than relative."[127] Certainly the market is an imperfect mechanism of such coordination. But it remains to be shown that central planning can in practice do anything but hinder this imperfect coordinating mechanism.

Maurice Dobb. We have already had two occasions to discuss Dobb as a participant of the calculation debate, in noting Bergson's treatment of Dobb's more centralized alternative to market-socialism, and Ward's analysis of his critique of the static market-socialist model. From these discussions, Dobb might be expected, as the historian of the debate, to have a sharply divergent view of the controversy, unlike either Austrian or neoclassical interpretations. However, in many ways Dobb's interpretation of the controversy is strikingly similar to the standard account, and his approach to the question of going beyond the static nature of the market-socialist model has its counterpart in a large body of modern neoclassical central planning theory.

Dobb clearly interprets Mises as having made a static equilibrium argument and agrees with the usual view that on this level he was effectively answered by the market-socialists.[128] He also subscribes to the "second line of defence" interpretation of Hayek, as well as the view that this "impracti-

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cability" argument can be disposed of by reference to modern computing techniques, linear programming methods, and the like. Indeed, despite his at times brilliant critique of the static nature of neoclassical economics, he seems to have quite uncritically adopted the standard neoclassical view as an answer to the Austrian challenge.[129]

Although we have been critical of this standard view for having trivialized the problem of imputation, Dobb's view is that imputation is even *more* simple than the market-socialists in the debate were willing to admit.

> There was a simple answer to those who maintained the necessity of a market for intermediate goods and for capital, to which surprisingly little attention was paid. It was that on their own showing the prices of such goods were derived from those of the finished goods that the former helped to make. If there was a retail market for consumption goods, why have a market for intermediate goods as well? If the latter could anyhow only acquire a price by an elaborate process of imputation, after they had been allocated in a certain way, why not allocate them according to the principle of directing them to the use where their productivity (at the margin) was greatest, without the added complication of pricing them?[130]

Thus Dobb accepted Lange's argument that it would be possible to have rational economic calculation without markets in capital goods and took this one step further in arguing that it would be possible even without prices for capital goods. Dobb does not explain how a plant manager could know whether his marginal productivity for any factor was optimized without knowing the prices of the various resources he is attempting to combine efficiently. He believes, in any case, that the complexity of this task has been greatly exaggerated and can be overcome by breaking down decisions into a hierarchy so that the CPB need only make broad macroeconomic decisions and delegate more microeconomic decisions to subordinates in the hierarchy.

> The present reviewer has never been convinced that the complexity would be as great as is alleged, provided that scope were given for decentralization of *particular* decisions inside the limits set by the shape of a *general* plan.[131]

This idea of allowing discretion over particular details while maintaining a central plan for macroeconomic direction of the economy requires that the nature of these decisions be such as to permit this hierarchy. However, the details Dobb is relinquishing to lower levels are crucial matters of which the CPB would have to be continually aware if they intend to genuinely control social production. The CPB cannot first decide how much steel to have produced and then allow individual plant managers to choose what kind of steel for which specific purpose, since the former decision depends on the latter. In effect the retreat to the "planning" of broad macroecono-

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mic categories is the retreat from economic planning to interventionism. The day-to-day particular decisions about specific economic goods are the choices which must be guided by rational economic calculation if society is to produce with a modicum of efficiency. If these are relinquished to the separate choices of decentralized plant managers the whole rationale for central planning goes with it.

Though it is Dobb's intention to get beyond the level of static analysis that he condemns the neoclassical economists for stressing, his own analysis retains the fundamental static assumptions of the neoclassical outlook (for example when he takes technology as "given" to each plant manager). His proposed theoretical path to escape static analysis is to adopt macroeconomic growth theory and pay less attention to the static efficiency ideal of welfare economics.

Dobb argues that since under dynamic assumptions it is quite impossible to achieve the perfection of equilibrium under either capitalism or socialism, it is not necessary for the CPB to try to strictly approximate this ideal. Considerations of static microeconomic efficiency, though certainly not entirely irrelevant, do not comprise the paramount issue for socialist economics. He charges market-socialists with what he calls the "Perfectibility Fallacy." He recommends that, rather than pursue this unattainable goal of Pareto-optimality, the CPB should focus on selecting and bringing about a higher overall rate of growth of the economy. In this way, he believes, socialism could attain such a high macroeconomic rate of growth that it could more than compensate for any deviations from microeconomic optima.

However, as Lerner pointed out in response to Dobb, this argument presupposes "that the two kinds of loss are alternative instead of additive" or, in other words, that growth can be improved by neglecting microeconomic efficiency.[132] The argument that perfect microeconomic efficiency as imagined in a general equilibrium model is unattainable does not yield the conclusion that processes of equilibration can be abandoned. Economic growth that is not closely linked with microeconomic efficiency considerations is an illusory goal.[133]

Frank Knight. One of the most significant features of the standard view of the calculation debate has been the conclusion usually drawn from it that "economic theory" *per se* cannot decide between capitalism and socialism. As Eduard Heimann put it in his *History of Economic Doctrines*, the debate about economic calculation "has confirmed once more the fact that the difference between the two systems is in social arrangements and psychological incentives rather than in purely economic issues."[134] Frank Knight was to make this the central point of his 1936 article on the calculation debate, where he contends that "The Place of Marginal Economics in an Collectivist System" is "not essentially different from its place in an economy of 'competitive individualism.'" This means that "the problems of collectivism

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are not problems of economic theory, but political problems, and that the economic theorist, as such, has little or nothing to say about them."[135]

Knight's view of the debate is especially interesting in that, while he was one of the most important developers and advocates of the perfect competition model, he was also one of the first to clearly point out its limitations. While "Part Two" of his *Risk, Uncertainty and Profit* is generally cited as Knight's great contribution to formal equilibrium analysis, his largely forgotten "Part Three" consists of an elucidation of what is missing in that formal theory. Equilibrium for Knight is that state in which no genuine uncertainty remains, and which thus contains no pure profit opportunities. The real world, by contrast, contains ineradicable elements of uncertainty, and thus numerous profit opportunities.

It is significant that Stigler in his introduction to this book discounts Knight's distinction between insurable risk and genuine uncertainty, a distinction that Austrian economists (and Knight himself) have considered a cornerstone of this work. Stigler is correct that "modern analysis no longer views the two classes as different in kind,"[136] but contemporary Austrians have specifically challenged modern economics on these grounds.[137] If all uncertainty were reducible to actuarial risk there could be no error, no learning, and thus no equilibrating process. All ignorance would be the result of a conscious decision to abstain from undergoing the known costs of acquiring missing pieces of information. Since we know that action in the real world is constrained by genuine ignorance of the future and, in particular, of one another's plans, the neoclassical model of choice as a maximization of given opportunities (or given probability distributions about such opportunities) is incomplete.[138] The element of action that is missing from this view has been called "entrepreneurship" by Mises and Kirzner, and an important rudimentary form of this idea is clearly contained in Knight's work.

Yet despite his important recognition of the difference between the perfect competition model and the real world, Knight insisted on identifying "economic theory" with such static equilibrium analyses. When he makes the statement that the "starting point" of his book was the "general conclusion that the existence of profit follows from a divergence between the conditions of theory and those of fact,"[139] one is led to consider the nature of that statement itself, or of his entire Part Three. Are these not theoretical statements? They are not formal equilibrium propositions; rather they describe the relationship between profit (a theoretical category) and such analysis. And we would argue also that they are clearly not matters entirely outside of economics (*i.e.*, belonging to the realm of politics, ethics, history, or some other discipline). This, however, is exactly how Knight treats these questions in his influential article on the calculation debate.

In that article, after having shown in the familiar manner how with given conditions a determinate stationary equilibrium can be proven for

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socialism as well as for capitalism, he points out that "reasoning on the assumption of stationary conditions can yield no conclusions of practical significance for economic policy, whatever the general pattern of economic organization." On this point, as we have shown, Mises and Hayek completely agree with Knight. But he goes on to say that "the facts of progressive change...take the discussion out of the realm of economics into that of politics."[140] While he has demonstrated why such facts take us out of the realm of static economics, he has not shown why economic theory must confine itself to static exercises, especially when Knight himself has not so confined his own contributions to economics.

This is not merely a question of semantics about what we call "economic theory." It involves a fundamental contrast between Knight and the Austrians over the proper theoretical role of equilibrium constructions. For Knight (at least in 1936) economic theory *is* equilibrium theory. In this view, which is implicit in many neoclassical discussions of the calculation debate, a "theoretical" economic argument against socialism, as Mises claimed he was making, will necessarily be interpreted as Lange interpreted it, as a static equilibrium argument, despite Mises' specific statement to the contrary.

Indeed, this was how Knight read Mises. Knight referred to Mises as "the academic opponent of socialism most conspicuous for the extremism of his position,"[141] and explicitly cited Mises as having asserted the existence of economic problems of socialism even under stationary conditions.[142]

For Mises and the Austrians in general, however, "economic theory" is a wider category that includes, but is by no means limited to, equilibrium analysis. After all, as Knight himself remarked on a different occasion, we are not directly concerned with equilibrium as a state of rest, but rather with "a process in equilibrium....The system never really is in equilibrium ('moving equilibrium') at any point; but its tendency toward such a state is the main feature to be made clear in a scientific description of it."[143] The static description of the equilibrium state of rest may be a useful analytical tool for explaining this "tendency," but it is the latter which is of primary concern.

For socialism to be theoretically sound from an economic point of view it must do more than fulfill Schumpeter's "logical credentials" under static assumptions. It must be theoretically demonstrated that socialist institutions can impel an equilibrating tendency without the existence of private ownership of capital.

In a later essay, while he still forcefully reiterates his point that "economic theory, as such, involves no disproof or rejection of socialism,"[144] Knight nevertheless finds himself in agreement with Mises' theoretical" argument when he relaxes his static assumptions:

> Thus the contention of Professor von Mises, and other opponents of socialism, that there would be no objective rationale for the organization

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> of production under socialism, while adequately refuted by Professor Lange (and others) for the routine operations of a stationary economy, is after all essentially correct for the really serious problem of organization. This is the problem of anticipating substantial changes in the given conditions of economic life and in making necessary adaptations and/or of bringing about such changes.[145]

This comment, unfortunately buried in a footnote at the end of an article ostensibly about the ethics of socialism, actually concedes Mises' whole point. Once it is recognized that Mises never intended to challenge the static "logical credentials" of socialism, Knight must be seen as a supporter of Mises' argument under the dynamic conditions of the real world. But, due to his stress on the formal similarity of capitalism and socialism under static conditions, Knight has been widely considered an opponent of Mises in the calculation debate.

Conclusion

In all of these accounts we repeatedly find the same neoclassical misinterpretation of Mises' challenge, the same emphasis on static equilibrium analysis, the same allegation of a "retreat" by Hayek and Robbins, the same conclusion that socialism is unassailable from the standpoint of "economic theory." However, the theory that is impotent in discussing the economics of central planning is the static neoclassical theory of the market-socialists and of the chroniclers of the debate we have been examining. The debate has been given a "non-innocent reading" by neoclassical theorists who have not yet appreciated the important differences between themselves and Austrian economists. When the Austrian challenge to socialism has been read by those who are familiar with the unique, dynamic quality of Austrian economic theory it has been recognized as a potent argument against central planning.

NOTES

1. See Ludwig von Mises, "Economic Calculation in the Socialist Commonwealth" (1920), trans. S. Adler, reprinted in F. A. Hayek, ed., *Collectivist Economic Planning: Critical Studies on the Possibilities of Socialism* (London: George Routledge and Sons, 1935); *idem, Socialism: An Economic and Sociological Analysis,* trans. J. Kahane (1922; London: Jonathan Cape, 1936); Hayek, "The Nature and History of the Problem" (1935), reprinted in Hayek, *Individualism and Economic Order* (Chicago: University of Chicago Press, 1948); *idem,* "The Present State of the Debate" (1935), reprinted in *Individualism and Economic Order; idem,* "The Competitive 'Solution'" (1940), reprinted in *Individualism and Economic Order;* Lionel Robbins, *The Great Depression* (New York: Macmillan, 1934) and *idem, Economic Planning and International Order* (London: Macmillan, 1937). Other early contributions which made arguments similar to Mises' include: N. G. Pierson, "The Problem of Value in the Socialist Community" (1902), trans. G. Gardiner, in Hayek, *Collectivist Economic Planning;* Max Weber, *Wirtschaft und Gesellschaft* (Tubingen, 1921); and B. Brutzkus, *Economic Planning in Soviet Russia* (1922; London: Routledge, 1935). We will concentrate mainly on the

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central Austrian contributions both because the market-socialist responses did so and because we find them to represent a more complete argument.

2. See Oskar Lange, "On the Economic Theory of Socialism" (1936), reprinted in Benjamin E. Lippincott, ed., *On the Economic Theory of Socialism* (1938; New York: McGraw Hill, 1964); H. D. Dickinson, "Price Formation in a Socialist Community," *Economic Journal* (June 1933); *idem, Economics of Socialism* (London: Oxford University Press, 1939); Fred M. Taylor, "The Guidance of Production in a Socialist State" (1929), reprinted in Lippincott, *On the Economic Theory;* Abba P. Lerner, "Economic Theory and Socialist Economy," *Review of Economic Studies* 2 (October 1934); *idem,* "A Note on Socialist Economics," *Review of Economic Studies* (October 1936); *idem,* "Statics and Dynamics in Socialist Economics," *Economic Journal* (June 1937); *idem, The Economics of Control: Principles of Welfare Economics* (New York: Macmillan, 1944); E. F. M. Durbin, "Economic Calculus in a Planned Economy," *Economic Journal* 46 (December 1936); *idem, Problems of Economic Planning* (London: 1949); Maurice Dobb, "Economic Theory and the Problems of a Socialist Economy," *Economic Journal* 43 (December 1933); and *idem,* "Saving and Investment in a Socialist Economy," *Economic Journal* 49 (December 1939).
3. See Taylor, "The Guidance of Production."
4. See Israel M. Kirzner, *Competition and Entrepreneurship* (Chicago: University of Chicago Press, 1973); *idem, Perception, Opportunity and Profit: Studies in the Theory of Entrepreneurship* (Chicago: University of Chicago Press, 1979). It should be made clear at the outset that the terms "Austrian" and "neoclassical" used in this study may not be consistent with common usage. For example, Schumpeter is not considered an "Austrian" for the purposes of this paper despite the Austrian flavor of much of his work, since on the issue of the calculation debate he adopts what we call a neoclassical view. Similarly the "flaws" in the "neoclassical" perspective cannot be attributed to every contemporary theorist who considers himself an heir to Walras and Marshall, and indeed may not have been contained in the original neoclassical theorists themselves. Rather we are referring to a tendency of many economists, notably the market-socialists, to take the formal equilibrium theory too seriously. Those neoclassical economists who see this formal theory as providing heuristic aids to economics may be closer to what we call the Austrian point of view. Most histories of thought treat this Austrian tradition—including Menger, Wieser, and Böhm-Bawerk—as a parallel development of marginalist/subjectivist economics with Jevons and Walras, and it seems that this was the view of the Austrians themselves at the time of the debate. However, much of what appeared to be subtle differences of expression has evolved into major issues of contention between Austrian and neoclassical perspectives.
5. For the best overall summary to date of the debate from this alternative perspective in English, see T. J. B. Hoff, *Economic Calculation in the Socialist Society* (London: William Hodge, 1949). Elements of this interpretation can be found in: D. T. Armentano, "Resource Allocation Problems Under Socialism," in William P. Snavely, ed., *Theory of Economic Systems: Capitalism, Socialism, and Corporatism* (Columbus, Ohio: Charles E. Merrill, 1969); James M. Buchanan, *Cost and Choice: An Inquiry in Economic Theory* (Chicago: University of Chicago Press, 1969); Michael Ellman, "The Fundamental Problem of Socialist Planning," *Oxford Economic Papers;* Georg Halm, "Further Considerations on the Possibility of Adequate Calculation in a Socialist Community," trans. H. E. Batson, in Hayek, *Collectivist Economic Planning; idem, Economic Systems: A Comparative Analysis* (New York: Holt, Rinehart and Winston, 1951); Hayek, *Collectivist Economic Planning; idem, New Studies in Philosophy, Politics, Economics and the History of Ideas* (Chicago: University of Chicago Press, 1978), pp. 232–46; W. H. Hutt, "Economic Institutions and the New Socialism," *Economica* (November 1940); Don Lavoie, "Rivalry and Central Planning: Toward a Reexamination of the Socialist Calculation Debate" (unpublished manuscript, New York University, 1980); G. Warren Nutter, "Markets Without Property: A Grand Illusion" (1968), reprinted in E. G. Furobotn and S. Pejovich, eds., *The Economics of Property Rights* (Cambridge, Mass.: Ballinger Publishing, 1974); Gerald P. O'Driscoll, Jr., *Economics as*

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a Coordination Problem: The Contributions of Friedrich A. Hayek (Kansas City: Sheed, Andrews, and McMeel, 1977); Vincent Ostrom, "Some Paradoxes for Planners: Human Knowledge and Its Limitation," in *The Politics of Planning: A Review and Critique of Centralized Economic Planning* (San Francisco: Institute for Contemporary Studies, 1976); Svetozar Pejovich, "The End of Planning: The Soviet Union and East European Experiences," in *ibid.;* Sir Arnold Plant, "Centralize or Decentralize" (1937), reprinted in Plant, *Selected Economic Essays and Addresses* (London: Routledge and Kegan Paul, 1974); Paul Craig Roberts, *Alienation and the Soviet Economy* (Albuquerque, N.M.: University of New Mexico Press, 1971); Murray N. Rothbard, *Man, Economy, and State: A Treatise on Economic Principles* (Los Angeles: Nash Publishing, 1962); *idem,* "Ludwig von Mises and Economic Calculation under Socialism," in Laurence S. Moss, ed., *The Economics of Ludwig von Mises: Toward a Critical Reappraisal* (Kansas City: Sheed and Ward, 1976); David Ramsay Steele, "The Impossibility of Communism" (unpublished manuscript, University of Hull, England, 1978); G. F. Thirlby, "The Ruler" (1946), reprinted in J. M. Buchanan and G. F. Thirlby, eds., *L.S.E. Essays on Cost* (London: Weidenfeld and Nicolson, 1973); Karen Vaughn, "Economic Calculation under Socialism: The Austrian Contribution," *Economic Inquiry* (Summer 1980); Jack Wiseman, "Uncertainty, Costs, and Collectivist Economic Planning" (1953), reprinted in Buchanan and Thirlby, *L.S.E. Essays; idem,* "The Theory of Public Utility Price—An Empty Box" (1957), reprinted in *ibid.*

6. Lekachman's comment that early Marxism "gave no notion of how the future socialist society would be organized" reflects the standard view on this issue (Robert Lekachman, *A History of Economic Ideas* [New York: Harper and Bros., 1959], p. 394).
7. Although the fact of the failure of War Communism is rarely denied, many accounts blame this on exogenous causes rather than on the deliberate policy of the Lenin regime to destroy market relations and the use of money. Köhler, for example, refers to War Communism as "a period of general confusion, civil war, and popular unrest about the widespread use of brutal force" (H. Köhler, *Welfare and Planning: An Analysis of Capitalism versus Socialism* [New York: John Wiley and Sons, 1966], p. 124). But the view that is more often expressed is that the Soviet regime was in error, at least with respect to the attempt to abolish money. Thus Dobb conceded that "it can be taken as tolerably certain that the difficulties of 'War Communism,' amounting in some cases almost to disaster, which were so vividly in evidence in 1920, were not merely incidental to the system," and he refers to the destruction of money as a key factor in this failure (Dobb, *Russian Economic Development Since the Revolution* [New York: Dutton, 1928], pp. 130–31). Other writers who were not at all sympathetic to the Mises-Hayek argument nevertheless admit that a completely moneyless economy cannot work and cite this period in Russian history to illustrate the point. See for example: Barbara Wootton, *Plan or No Plan* (New York: Farrar and Rinehart, 1935); and Baidyanath Misra, *Capitalism, Socialism and Planning* (New Delhi: Oxford and IBH Publishing, 1972), p. 139. For an excellent account of the period that is consistent with our interpretation of the calculation debate, see the contributions by Roberts, "War Communism: A Re-examination," *Slavic Review* (June 1970); and *idem, Alienation and the Soviet Economy.*
8. Lavigne contends that the idea that "plan and market are mutually exclusive... was developed mainly by contemporary liberal economists during the early period of socialism in Soviet Russia" and refers to Mises and Hayek in this regard. See Marie Lavigne, *The Socialist Economies of the Soviet Union and Europe,* trans. T. G. Waywell (White Plains, N.Y.: I.A.S.P., 1974), pp. xii, 377. Others have also tried to deny that this model of socialism is implicit in Marx, including: Ernest Mandel, *Marxist Economic Theory,* trans. Brian Pearce (1962; New York: Monthly Review Press, 1970), pp. 632–33; Lange, "Marxian Economics and Modern Economic Theory," *Review of Economic Studies* 2 (1934–1935); and *idem,* "Marxian Economics in the Soviet Union," *American Economic Review* 35 (March 1945). We would argue, however, that they have not been very convincing. See for example: Lavoie, "Marx's Socialism and Mises' Challenge" (unpublished manuscript, New York University, 1980); Roberts, *Alienation and the Soviet Economy;* and Steele, "The Impossibility of Communism."

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9. A common Marxist interpretation of Karl Marx's comments on the two "phases" of communism as discussed in his 1891 "Critique of the Gotha Programme" (reprinted in *The First International and After: Political Writings,* vol. 3, ed. D. Fernbach [New York: Random House, 1974]), is that the first phase, now called "socialism," employs money, market exchange, and a price system; while the second phase, full communism, in which the slogan "from each according to his ability, to each according to his needs" can be realized, no longer faces the problem of scarcity. We would argue that this interpretation is fundamentally mistaken about Marx's first phase, which, by our account, explicitly eschews the use of money. Thus we contend that a substantial literature on the "transition period" in contemporary Marxism is entirely misconceived, since it starts from the mistaken idea that Marxian socialism in its first phase has already arrived in twentieth-century "socialist" countries. See Adam Buick, "The Myth of the Transitional Society" (1975), *Critique,* no. 5.
10. An exception to this common view is Blodgett, who argues that Mises' claim that planning without a market would be arbitrary has become accepted by "ever so many economists" (Ralph H. Blodgett, *Comparative Economic Systems* [1944; New York: Macmillan, 1979], pp. 133–47). It seems that Blodgett has in mind the first "retreat" of the debate (from Marxism to market-socialism), while most commentators on the controversy are referring to the second "retreat" (from Mises' "theoretical" to Hayek's "practical" argument against socialism), when they say Mises was wrong.
11. The usual method by which Mises' ideas are presented is to first briefly state his argument and to then offer a detailed digression on equilibrium theory and welfare economics. Thus Howard J. Sherman (*The Soviet Economy* [Boston: Little, Brown & Co., 1969], pp. 262–63, 268) writes: "An evaluation of Mises' objection requires a brief explanation of how economists define 'rational' prices and 'rational' planning. Rational prices are defined as those which lead to an 'optimal' pattern of outputs and inputs, by the accurate representation of the marginal utility of each output and the marginal cost of each input. As early as 1897 the economist Pareto made explicit the conditions necessary to obtain an optimum welfare situation for all individuals, given the existing technology and the existing distribution of income.

"We should be aware that Mises and Hayek attack the actual or realized operation of an imperfect planned socialist system from the viewpoint of a pure and perfect competitive private enterprise system."

C. Bliss ("Prices, Markets, and Planning," *Economic Journal* [March 1972], p. 91) and Carl Landauer (*Theory of National Economic Planning* [Berkeley: University of California Press, 1947], pp. 56–57) similarly translate Mises' argument into Walrasian terms, while the perfect competition assumption that all agents are price-takers is attributed to the Mises-Hayek position by Köhler (*Welfare and Planning,* p. 72) and Misra (*Capitalism,* pp. 140–45). The word "efficiency" is invariably understood by neoclassical theorists to mean "Pareto-optimality," as, for example, in: R. Eidem and Staffan Viotti, *Economic Systems* (New York: John Wiley and Sons, 1978), p. 76; and Shanti S. Tangri, ed., *Command versus Demand: Systems for Economic Growth* (Boston: D. C. Heath, 1967), pp. vi–vii.
12. See for example: R. A. Dahl and D. E. Lindblom, *Politics, Economics, and Welfare: Planning and Politico-Economic Systems Resolved into Basic Social Processes* (New York: Harper & Row, 1953), pp. 210–11; Jan Drewnowski, "The Economic Theory of Socialism: A Suggestion for Reconsideration," *Journal of Political Economy* (August 1961); John E. Elliot, *Comparative Economic Systems* (Englewood Cliffs, N. J.: Prentice-Hall, 1973), p. 243; Köhler, *Welfare and Planning,* p. 68; Landauer, *Theory of National,* p. 52; Tangri, *Command versus Demand,* p. vi. The impulse to so interpret Mises is so strong that it sometimes persists alongside powerful contradictory evidence. Thus, Snavely's *Theory of Economic Systems* contains a clear essay by Armentano ("Resource Allocation Problems Under Socialism") that explains how Mises "notes...that economic calculation ceases to be a problem in the stationary state or in equilibrium. But he considers this fact to be quite irrelevant to the problem of economic calculation under socialism, since 'equilibrium' is an imaginary construct and certainly

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not obtainable in a real world where economic data change and uncertainty exists."

Nonetheless, Snavely proceeds to repeat the same neoclassical version of Mises ten pages later in the book: "Lange next turned his attention to the arguments of Hayek and Robbins who, unlike Mises, accepted the theoretical possibility of Barone's approach...."

Similarly, Marshall I. Goldman, in *Comparative Economic Systems: A Reader* (1964; New York: Random House, 1971), p. 11, repeats the standard account despite his inclusion four pages later of excerpts from Mises' *Socialism* (pp. 119–22, 137–42), in which the latter expressly states that socialism could work in theory under static conditions.

13. For example, see Misra, *Capitalism,* p. 188; and Tangri, *Command versus Demand,* pp. vii–viii.
14. Elliot (*Comparative Economic Systems,* p. 293) refers to the contemporary consensus that Mises was wrong, citing Joseph A. Schumpeter, *Capitalism, Socialism and Democracy* (New York: Harper & Row, 1942), in this regard, and concludes: "Private ownership is not now regarded as a *logically necessary* requisite for the existence of a pricing system as a social process for economic calculation." Referring to Lange's model, Dahl and Lindblom (*Politics, Economics, and Welfare,* p. 211) say: "As an analytical model in economic theory, this picture of a socialist price system is valid; the consensus of economists is that Von Mises was wrong in not granting at least this much." Köhler (*Welfare and Planning,* p. 69) agrees that "clearly...Von Mises had gone too far."
15. The standard view of the significance of Barone's argument is contained in such works as: Köhler, *Welfare and Planning,* p. 69; Lekachman, *A History of Economic Ideas,* pp. 394–95; Ban B. Seligman, *Main Currents in Modern Economics* (1962; Chicago: Quadrangle, 1971), 1:107–108; and Sherman, *The Soviet Economy,* p. 264.
16. Goldman (*Comparative Economic Systems,* p. 11) writes: "Initially the argument focused around the feasibility of one system versus another. It was eventually accepted that both the Lange-Lerner and input-output systems could theoretically answer the economic question about the allocation of resources and manpower. Then the debate shifted to a dispute over which solution would be the most efficient one."

Misra (*Capitalism,* pp. 131, 140) is unclear in his interpretation of Mises, but implies the standard view on the second "retreat" when he explains that Hayek and Robbins "have pointed out that while a mathematical solution is theoretically correct, it does not provide a practical method of deciding how to use capital equipment."

Landauer (*Theory of National,* p. 57) writes: "Hayek, relinquishing the old Mises position, conceded the formal possibility of planning, but maintained that the planning board would never finish solving the innumerable equations through which the value of individual commodities would have to be calculated."

Sherman (*The Soviet Economy,* p. 265): "In the next stage of the debate, Hayek admits that *in theory* the planners might accumulate all the millions of pieces of necessary information and might then solve all the millions of equations necessary to make an optimal decision. *In practice,* Hayek argues, no conceivable force of planners could actually gather all of the various kinds of information from every factory and farm, and from every private and public consumer. Furthermore, *in practice,* even with all of the information, it would take hundreds of years to solve correctly all of the equations for just one year's plan."

See also Elliot, *Comparative Economic Systems,* p. 243; Seymour E. Harris, *Economic Planning: The Plans of Fourteen Countries with Analysis of the Plans* (New York: Alfred A. Knopf, 1949), p. 5; Köhler, *Welfare and Planning,* p. 79; and Tangri, *Command versus Demand,* p. vi.
17. Goldman (*Comparative Economic Systems,* p. 10) argues that Lange and Lerner provided "an answer acceptable to economists" when they "decided to meet von Mises on his own terms." I. M. D. Little (*Critique of Welfare Economics* [Oxford: Clarendon Press, 1950], p. 254) concurs: "Thus, and with some irony, the static welfare-theory armament of the supporters of *laissez-faire* was seized by their opponents, and effectively used against them."

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18. Harris (*Economic Planning,* p. 4) and G. M. Pickersgill and J. E. Pickersgill (*Contemporary Economic Systems: A Comparative View* [Englewood Cliffs, N.J.: Prentice-Hall, 1974], p. 306) use the word "demonstrated" to describe Lange's answer to the Mises argument. Seligman (*Main Currents,* p. 109) calls the market-socialist approach "the definitive response," while I. H. Rima (*Development of Economic Analysis* [Homewood, Ill.: Richard D. Irwin, 1972], pp. 350–51) refers to Lange's "proof." Little (*Critique of Welfare Economics,* p. 253) contends that "at a logical level [Mises'] challenge was completely answered by socialist economists, principally Mr. Lange and Professor Lerner."

    Lekachman (*A History,* pp. 396–97): "Oskar Lange. . . proved that a Central Planning Board could impose rules upon socialist managers which allocated resources and set prices as efficiently as a capitalist society of the purest stripe, and much more efficiently than the capitalist communities of experience."

    Landauer (*Theory of National,* p. 51): "These socialist authors, primarily Oskar Lange and H. D. Dickinson, have done an excellent job in refuting some of the arguments by which the possibility of value calculation without the institution of a market had been denied. They showed clearly that the 'real' process through which the market arrives at an equilibrium price and the calculating process which a central agency must apply for the same purpose have traits in common which make it impossible to question the practicability of advance calculation of values by a planning board."

    Heilbroner (*Between Capitalism and Socialism: Essays in Political Economics* [New York: Random House, 1970], p. 88), after summarizing the Mises-Hayek argument, concludes that "This line of attack against socialism did not fare very well. In the mid-1930s it was effectively demolished by Oscar Lange, the brilliant Polish economist then at Harvard.

    "Lange demonstrated. . . that a Central Planning Board could indeed plan rationally for the simple reason that it would receive exactly the same information from a socialized economic system as did entrepreneurs under a market system."

19. Although confident assertions that the Lange model is valid "in theory" or "as a model"—such as Dahl and Lindblom, *Politics, Economics and Welfare,* p. 211; and Köhler, *Welfare and Planning,* pp. 69, 71—abound in comparative economics texts, it is frequently admitted that this model may not be workable in reality. Earl R. Sikes (*Contemporary Economic Systems—Their Analysis and Historical Background* [New York: Henry Holt and Company, 1940], p. 280) remarks that Lange's solution "may be a basis for economic calculation, but it is scarcely a basis for effective economic planning." Lekachman (*A History,* p. 397), after having expressed the view that Mises had been proven wrong, goes on to say that: "It need scarcely be said that economic planning in Russia, or anywhere else, fails rather completely to conform to [Lange's] model," as if the evident impracticability of this solution was irrelevant to its potency against Mises.
20. Because the standard view of the debate stresses the formal similarity of capitalism and socialism under static assumptions, and believes this to have been the analytical framework of the whole controversy, the conclusion is usually expressed that both economic systems are equally valid "in theory." Thus Herbert Hugo Liebhafsky (*The Nature of Price Theory* [Homewood, Ill.: Dorsey, 1963]) emphasizes the idea that exactly the same (static) welfare conditions apply to each; and G. Dalton (*Economic Systems and Society: Capitalism, Communism and the Third World* [Harmondsworth: Penguin, 1974], p. 135) says that Lange, Lerner, and Taylor showed that the rules for optimization are general. Sherman, in *The Soviet Economy* (pp. 267–68) writes: "If there is pure and perfect competition under market socialism, it turns out that the resulting allocation of resources is exactly as efficient as under pure and perfect competition in private enterprise.

    "When we examine the pure and perfect form of each of these, we find that *in theory* they are equally capable of reaching a Pareto optimum condition."

    Jesse Markham, in his short "editor's introduction" to Alan G. Gruchy's *Comparative Economic Systems: Competing Ways to Stability and Growth* (Boston: Houghton Mifflin, 1966), p. v (that book's only reference to the calculation debate), can find little

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of value in the controversy's "rather bland intellectual diet of 'theoretical' capitalism and socialism," in which "Advocates of private enterprise typically argued that, in theory, a freely functioning market economy could assure society of economic efficiency without exacting the price of bureaucratic bungling, caprice, or plain stupidity, the inevitable concomitants of socialistic central planning. Proponents of socialism, with equal irrelevance, argued that the smoothly functioning blueprint of central planning boards eliminated the injustices and inefficiencies of private monopoly power and restraints on trade, the inescapable features of capitalistic economies. Since almost any system in theory can be made to appear superior to another system in practice, the debate was at best unrewarding and at worst misleading."

Theo Suranyi-Unger (*Comparative Economic Systems,* [New York: McGraw-Hill, 1952], p. 40) remarks that in the debate "some of the abstract results have been splendid. Yet they have been largely confined to the realm of economic theory." Similar comments that pure theory is sterile can be found in the accounts of the debate by Blodgett, *Comparative Economic Systems,* p. 147; Dahl and Lindblom, *Politics, Economics, and Welfare,* p. 20; Eidem and Viotti, *Economic Systems,* pp. 92–93; Elliot, *Comparative Economic Systems,* p. 233; and Köhler, *Welfare and Planning,* pp. 4–5.

21. Two interesting critiques of welfare economics from Austrian and Marxian perspectives can be found in Murray N. Rothbard, "Toward a Reconstruction of Utility and Welfare Economics," *Occasional Paper Series,* no. 3 (New York: Center for Libertarian Studies, 1977); and Dobb, *Welfare Economics and the Economics of Socialism: Toward a Commonsense Critique* (Cambridge: Cambridge University Press, 1969). Attempts have been made to develop a "measure" of static efficiency in Gerard Debreu, "The Coefficient of Resource Utilization," *Econometrica* 19 (July 1951); and T. C. Koopmans and J. M. Montias, "On the Description and Comparison of Economic Systems," in Alexander Eckstein, ed., *Comparison of Economic Systems: Theoretical and Methodological Approaches* (Berkeley: University of California Press, 1971), p. 44.
22. See Paul A. Baran, "National Economic Planning," in B. F. Haley, ed., *A Survey of Contemporary Economics* (Homewood, Ill.: Richard D. Irwin, 1952), 2:386; Bliss, "Prices, Markets, and Planning," pp. 95–99; Dahl and Lindblom, *Politics, Economics, and Welfare,* p. 211; Dobb, *On Economic Theory and Socialism: Collected Papers* (London, 1955), pp. 60, 241–43; E. K. Hunt and J. G. Schwartz, eds., *Critique of Economic Theory* (London: Penguin, 1972); Köhler, *Welfare and Planning,* p. 78; William N. Loucks, *Comparative Economic Systems* (New York: Harper and Bros., 1957), p. 263; Edward J. Nell, "The Fall of the House of Efficiency," *Annals of the American Academy of Political and Social Science* 409 (September 1973); Roy Radner, "Competitive Equilibrium under Uncertainty," *Econometrica* 36 (1968); Alex Rubner, *Three Sacred Cows of Economics* (London: MacGibbon and Kee, 1970), pp. 206–208; G. L. S. Shackle, *Epistemics and Economics: A Critique of Economic Doctrines* (Cambridge: Cambridge University Press, 1972), p. 270; and Thorstein Veblen, *The Place of Science in Modern Civilization, and Other Essays* (New York: Viking Press, 1919).
23. Sikes (*Contemporary Economic Systems,* p. 281) asserts that "planning. . . has possibilities of regularizing production not present under capitalism"; and Misra (*Capitalism, Socialism and Planning,* p. 151) claims more specifically that the socialist state "has greater capacity to forecast" and "control uncertainty."

Robert A. Solo (*Economic Organizations and Social Systems* [Indianapolis, Ind.: Bobbs-Merrill, 1967], pp. 48–50, 66–67) develops the notion of "internal uncertainty" which is due to the decentralization of decision-making, and which can therefore be potentially eliminated under centralized economic schema. Solo writes: "Under decentralized market-direction, components of related economic processes are organized as separate, independent decision-making agencies. Although the activities of these agencies are interdependent, each must chart its course of action without knowing the anticipations, intentions, and plans of the others. Thus decentralized decision-making generates pervasive and costly uncertainties. The centralization of choice eliminates the necessity for internal uncertainty." He does admit, however, (*ibid.,* p. 48), that there are

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some kinds of uncertainties which "escape prediction and elude foresight under any form of economic organization." In particular he points out that the central planning apparatus may be ill-suited for the kind of experimentation entrepreneurs engage in under a decentralized system: "The plan is the antithesis of experiment. The plan arranges, fixes, gears all the parts together. Experiment disarranges. Experiment is an exercise in the uncertain, a rendezvous with the unknown. But the virtue of the plan is that it is known, that it is clearly, cleanly intermeshed, that it rolls out uncertainties" (*ibid.*, pp. 149–50). To reach the conclusion that central planning may be less capable than capitalism of coping with uncertainty, it need only be added to Solo's discussion that economic production in an advanced economy is essentially a network of continuous experimentation.

E. Neuberger and W. Duffy (*Comparative Economic Systems: A Decision-Making Approach* [Boston: Allyn and Bacon, 1976], p. 96) argue that the advantage of more centralized over less centralized systems is that in the former "the optimal solution can be reached more rapidly, thereby avoiding a waste of resources and the possibility of disequilibrating dynamic processes leading to divergence rather than convergence."

Landauer (*Theory of National,* pp. 64–63) has a similar idea in mind when he contends: "It is a crude method to search for an equilibrium by experimentally varying all the determinants until they fit together, and. . .it is infinitely more economical to carry out these variations on paper than in reality." He argues that "in an unplanned economy we cannot get very far by paper calculation, because we know too little about the reactions of others to the same problem" (*ibid.*, p. 60). Only when these reactions are constrained by a prior conscious plan can such "internal uncertainties" be eliminated. But, as Solo pointed out, this can only be accomplished at the expense of experimental discovery.

24. Many discussions, after pronouncing economic theory incapable of judging capitalism versus socialism, resort to ethical and psychological issues such as whether bureaucrats will be given enough "incentives" or "motivation" to fulfill the rule-following tasks Lange assigns them. See Timothy W. Costello, "Psychological Aspects: The Soft Side of Policy Formation," *Policy Sciences* 1 (1970); Köhler, *Welfare and Planning,* pp. 78–79; and Pickersgill and Pickersgill, *Contemporary Economic Systems,* p. 310. Although the question of incentives is closely connected to the calculation argument, it is related in a way that is quite distinct from matters of psychology and more appropriately considered matters of the theory of ownership in economics and law.

    A similar reaction to the presumed impotence of economic theory is the insistence that economists turn their attention to "empirical" work instead. For example, when Bela A. Balassa (*The Hungarian Experience in Economic Planning* [New Haven, Conn.: Yale University Press, 1959], p. 17) concludes that "economic arguments are not sufficient to make a choice between economic systems," he suggests that we study the facts instead. We would agree with the spirit of this remark, but when theoretical confusion runs as deep as it does in the calculation debate there is not the barest analytical framework with which to begin a study of the "facts." The result in practice is that empirical studies smuggle implicit theoretical assumptions into their work.

25. The following comment by Bliss ("Prices, Markets, and Planning," p. 92) is typical: "The protagonists on both sides were debating, without realizing it, about the Economics of Fairyland, and different Fairylands at that."

26. See Dahl and Lindblom, *Politics, Economics and Welfare,* p. 4; Dalton, *Economic Systems and Society,* p. 112; and Eugene O. Golob, *The "ISMS", a History and Evaluation* (New York: Harper and Bros., 1954). Eckstein (*Comparison of Economic Systems,* p. 3) concludes that the calculation debate led to an increasing recognition that the preoccuption with comparisons based on "isms" was likely to yield overly simple and simplistic insights into the character of economic systems. In contrast, comparisons of models and realities tended to focus on the complexity and variety of living systems and their departure from the theoretical ideal.

    Suranyi-Unger, in *Comparative Economic Systems,* goes so far as to call for "A Crusade against 'Isms'" (the title of his section one, chapter five).

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A very diverse group of economists, from transition-Marxists to post-Keynesians to neoclassical welfare economists, agree that central planning consists of a judicious mixture of centralized decision-making with market institutions. Janos Korani (*Overcentralization in Economic Administration: A Critical Analysis Based on Experience in Hungarian Light Industry,* trans. John Knapp [Oxford: Oxford University Press, 1959], p. 255) makes a typical comment: "In principle it is possible to sketch out a system in which all economic choices, including even the distribution of consumer goods to individuals and people's choices of occupation, are governed by instructions from the centre. It is also possible to imagine a system in which the central authorities of the State refrain completely from all interference in economic life, everything being governed by the market mechanism. In practice, some mixture of these two is the inevitable rule. . . . This is also true in regard to socialist economies based on public ownership of the means of production."

See, for example, Morris Bornstein, ed., *Plan and Market* (New Haven, Conn.: Yale University Press, 1973); W. Brus, *The Market in a Socialist Economy* (London: Routledge and Kegan Paul, 1972); *idem, Socialist Ownership and Political Systems,* trans. R. A. Clarke (London: Routledge and Kegan Paul, 1975); J. T. Dunlop and N. P. Fedorenko, eds., *Planning and Markets: Modern Trends in Various Economic Systems* (New York: McGraw-Hill, 1969); W. Friedman, *Public and Private Enterprise in Mixed Economies* (New York: Columbia University Press, 1974); Eduard Heimann, "Planning and the Market System," in Findlay MacKenzie, ed., *Planned Society: Yesterday, Today, Tomorrow* (New York: Prentice-Hall, 1937); M. Kaser and R. Portes, eds., *Planning and Market Relations* (London: Macmillan, 1971); I. Konnik, "Plan and Market in the Socialist Economy," *Problems of Economics* (December 1966); Landauer, *Theories of National,* pp. 36–40; *idem, Contemporary Economic Systems: A Comparative Analysis* (Philadelphia: J. B. Lippincott, 1964); Lange, ed., *Problems of Political Economy of Socialism* (New Delhi, 1962); Wayne A. Leeman, ed., *Capitalism, Market Socialism and Central Planning* (Boston: Houghton Mifflin, 1963); Eugen Loebl, *Humanomics: How We Can Make the Economy Serve Us—Not Destroy Us* (New York: Random House, 1976); Mandel, *Marxist Economic Theory,* p. 636; Herbert Marcuse, *Soviet Marxism: A Critical Analysis* (1958; New York: Random House, 1961), p. 151; John Michael Montias, "Socialist Price Systems," *American Economic Review* 53 (March and December 1963); Gunnar Myrdal, *Beyond the Welfare State: Economic Planning and Its International Implications* (New Haven, Conn.: Yale University Press, 1960), p. 15; Krzysztof Porwit, *Central Planning: Evaluation of Variants,* trans. Jozef Stadler (Oxford: Pergamon Press, 1967); Ota Sik, *Plan and Market Under Socialism* (White Plains, N.Y.: IASP, 1967); *idem,* "Socialist Market Relations," in C. H. Feinstein, ed., *Socialism, Capitalism, and Economic Growth: Essays Presented to Maurice Dobb* (Cambridge: Cambridge University Press, 1967); *idem, The Third Way: Marxist-Leninist Theory and the Modern Industrial Society,* trans. M. Sling (1972; White Plains, N.Y.: IASP, 1976), pp. 193–95; Sh. Turetskii, "Price and Its Role in the System of Economic Methods of Management," *Problems of Economics* (May 1967); Alesky Wakar and J. G. Zielinsky, "Socialist Price Systems," *American Economic Review* 52 (March-December 1963); Wootton, *Plan or No Plan,* pp. 127–28; and J. A. Yunkar, "A Survey of Market-Socialist Forms," *Annals of Public and Co-operative Economy* (April-June 1975).

28. A voluminous literature in both the East and West has grown on this subject, the most notable Soviet contribution being L. V. Kantorovich, *The Best Use of Economic Resources* (Cambridge, Mass.: Harvard University Press, 1965). See also K. J. Arrow, L. Hurwicz, and H. Uzawa, *Studies in Linear and Non-linear Programming* (Stanford: Stanford University Press, 1958); William J. Baumol, "Activity Analysis in One Lesson," *American Economic Review* (December 1958); *idem, Economic Theory and Operations Analysis* (Englewood Cliffs, N.J.: Prentice-Hall, 1972), pp. 70–190, 294–318, 515–35; Mark Blaug, *Economic Theory in Retrospect* (London: Heinemann Educational Books, 1968), pp. 410–12; Robert W. Campbell, "Marx, Kantorovich, Novozhilov: 'Stoimost' versus Reality," *Slavic Review* (October 1961); H. B. Chenery and P. G. Clark, *Interindustry Economics* (New York: John Wiley and Sons, 1959); H. B. Chenery and K.

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29. See B. P. Beckwith, *The Economic Theory of a Socialist Economy* (Stanford, 1949);

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idem, Marginal Cost Price Output Control (New York: Columbia University Press, 1955); L. Ya. Berri, ed., *Planning Socialist Economy,* trans. Jenny Warren (1973; Moscow: Progress Publishers, 1977), pp. 115–47; H. Brems, *Output Employment, Capital and Growth* (New York, 1959); Brus, *Socialist Ownership,* p. 74; A. Chilosi, "The Theory of Growth of a Socialist Economy of M. Kalecki," *Economics of Planning* (1971); Dobb, "Saving and Investment"; *idem, An Essay on Economic Growth and Planning* (London, 1960); *idem, Papers on Capitalism; idem, Welfare Economics,* pp. 153–82; E. Domar, *Essays in the Theory of Economic Growth* (New York, 1957); Feinstein, *Socialism;* Goldman, *Comparative Economic Systems;* S. Gomulka, *Inventive Activity, Diffusion and the Stages of Economic Growth* (Aarhus, 1971); Gregory Grossman, "Soviet Growth: Routine, Inertia, and Pressure," *American Economic Review* (May 1960); G. C. Harcourt and N. F. Laing, eds., *Capital and Growth* (London: Penguin, 1971); Michael Harrington, *The Twilight of Capitalism* (New York: Simon and Schuster, 1976); A. R. G. Heesterman, *Allocation Models for National Economic Planning* (Dordrecht, Holland: D. Reidel, 1970); *idem, Forecasting Models for National Economic Planning* (Dordrecht, Holland: D. Reidel, 1970); Vaclar Holesevsky, "Karl Marx and Soviet National Income Theory," *American Economic Review* (May 1961); B. Horvat, "The Optimum Rate of Investment," *Economic Journal* (1958); *idem,* Towards a *Theory of Planned Economy* (Belgrade, 1964); *idem,* "The Optimum Rate of Investment Reconsidered," *Economic Journal* (1965); Michal Kalecki, *Selected Essays on the Economic Growth of the Socialist and the Mixed Economy* (Cambridge, 1972); T. Khachaturov, *Methods of Long-Term Planning and Forecasting* (London: Macmillan, 1976); Kornai, *Rush Versus Harmonic Growth* (Amsterdam: North-Holland, 1972); J. Kornai and T. Liptak, "Two-level Planning," *Econometrica* (January 1965); J. A. Mirrlees and N. H. Stern, eds., *Models of Economic Growth* (1970; New York: Wiley, 1973); Michio Morishima, *Marx's Economics: A Dual Theory of Value and Growth* (Cambridge: Cambridge University Press, 1973); *The Rate and Direction of Inventive Activity,* National Bureau of Economic Research (Princeton: Princeton University Press, 1962); G. Warren Nutter, *The Growth of Industrial Production in the Soviet Union* (Princeton: Princeton University Press, 1962); A. Parker, "On the Application of Mathematics in Soviet Economics," *Yale Economic Essays* 3 (Fall 1963); Sherman, *The Soviet Economy,* pp. 215–31, 266, 275; Sik, *Plan and Market,* p. 262; *idem, The Third Way,* p. 201; Vernon L. Smith, *Investment and Production: A Study in the Theory of Capital-using Enterprise* (Cambridge, Mass.: Harvard University Press, 1961); R. Stone and G. Stone, *National Income and Expenditure* (London: Bowes and Bowes, 1972); and J. Tinbergen and H. C. Bos, *Mathematical Models of Economic Growth* (New York: McGraw-Hill, 1962).

30. See Schumpeter, *History of Economic Analysis* (New York: Oxford University Press, 1954); and *idem, Capitalism, Socialism and Democracy.*
31. *Ibid.*, p. 172.
32. *Ibid.* It is worth noting that although many authorities who support the standard view of the debate cite these three writers—Pareto, Barone, and Wieser—as early expositors of the Lange position, all three in fact seriously questioned the practicability of socialist planning. See for example: Friedrich von Wieser, *Social Economics* (1914; London: Allen and Unwin, 1927), pp. 376–97.
33. Schumpeter, *Capitalism, Socialism and Democracy,* p. 175.
34. Schumpeter, *History of Economic Analysis,* p. 988. We will argue that the process by which the demand for factors is "derived" from the demand for consumers' goods is far more complex and problematic than the previous two somewhat naive quotes in the text imply. Schumpeter seems to believe that the derivation in practice is as trivial a matter as it is in formal equilibrium theory.
35. Schumpeter, *Capitalism, Socialism and Democracy,* pp. 175–76.
36. *Ibid.*, p. 177.
37. *Ibid.*, pp. 177, 180–81.
38. *Ibid.*, pp. 185–86.
39. Schumpeter, *History of Economic Analysis,* pp. 989–90.

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40. Schumpeter, *Capitalism, Socialism and Democracy,* p. 184.
41. *Ibid.*, p. 188.
42. Schumpeter, *History of Economic Analysis,* p. 989.
43. *Ibid.*, p. 987.
44. Benjamin N. Ward, *The Socialist Economy: A Study of Organizational Alternatives* (New York: Random House, 1967), p. 30.
45. Abram Bergson, "Socialist Economics," in Howard S. Ellis, ed., *A Survey of Contemporary Economics* (Homewood, Ill.: Richard D. Irwin, 1948), 1:412.
46. *Ibid.*, pp. 412–13.
47. *Ibid.*, pp. 413–20.
48. *Ibid.*, p. 420.
49. *Ibid.*
50. *Ibid.*, p. 421.
51. Bergson, "A Reformulation of Certain Aspects of Welfare Economics," *Quarterly Journal of Economics* 52 (February 1938). Also see F. M. Bator, "The Simple Analytics of Welfare Maximization," *American Economic Review* (March 1957); William J. Baumol, "Activity Analysis in One Lesson"; Bergson, "A Reformulation"; Peter Bohm, *Social Efficiency: A Concise Introduction to Welfare Economics* (New York: John Wiley and Sons, 1973); James M. Buchanan, "Knut Wicksell on Marginal Cost Pricing," *Southern Economic Journal* (October 1951); Ronald H. Coase, "The Marginal Cost Controversy," *Economica* 13 (August 1946); J. de V. Graaf, *Theoretical Welfare Economics* (Cambridge: Cambridge University Press, 1957); Hicks, "Foundations of Welfare Economics"; Harold Hotelling, "The General Welfare in Relation to Problems of Taxation and of Railway and Utility Rates," *Econometrica* 6 (1938); Michael Kaser, "Welfare Criteria," in Jane Degras, ed., *Soviet Planning: Essays in Honour of Naum Jasny* (Oxford: Basil Blackwell, 1964); Köhler, *Welfare and Planning;* Lange, "Foundations of Welfare Economics," *Econometrica* 10 (July-October 1942); Little, *Critique of Welfare Economics;* S. C. Littlechild, "The Problem of Social Cost," in Louis M. Spadaro, ed., *New Directions in Austrian Economics* (Kansas City: Sheed, Andrews and McMeel, 1978); James E. Meade, *The Just Economy: Principles of Political Economy* (London: Allen and Unwin, 1976); A. C. Pigou, *Economics of Welfare* (London, 1929); Nancy Ruggles, "The Welfare Basis of the Marginal Cost Pricing Principle," *Review of Economic Studies* 17 (1950); Thirlby, "The Marginal Cost Controversy: A Note on Mr. Coase's Model," *Economica* 14 (February 1947); *idem,* "Economists' Cost Rules and Equilibrium Theory," in Buchanan and Thirlby, *L.S.E. Essays;* P. Wiles, *Economic Institutions Compared* (New York: John Wiley and Sons, 1977); and Wiseman, "Uncertainty, Costs, and Collectivist Economic Planning."
52. Bergson, "Socialist Economics," pp. 428–29.
53. *Ibid.*, p. 433.
54. However, the question arises whether agents in such a world would even require anything like a "price system" in order to coordinate their almost entirely routine behavior with one another.
55. Hayek, "The Competitive 'Solution,'" p. 188.
56. Bergson, "Socialist Economics," p. 440.
57. Bergson, "Market Socialism Revisited," *Journal of Political Economy* 75 (October 1967): 662.
58. Mises, *Human Action: A Treatise on Economics* (London: William Hodge, 1949), p. 704. For the Austrians the coordination of plans resident in separate minds throughout an economy is the equilibrium which the "trial and error" procedure would have to attempt to "find," whereas the neoclassical conception of equilibrium is simply a quantitative matching of "supplies" to "demands."
59. Bergson, "Socialist Economics," p. 431.
60. Bergson is here quoting from Hayek's "The Use of Knowledge in Society," reprinted in Hayek, *Individualism,* p. 83.
61. Bergson, "Socialist Economics," pp. 436–37.
62. *Ibid.*, p. 435.

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63. *Ibid.*, p. 443.
64. For example, it is not helpful to the plant manager of a copper pipe factory to know that the average proportion of the total output of copper mines during a twenty-year span which was used in the "manufacturing" industry has been relatively stable. He is concerned with much narrower and more particular issues than input-output tables convey, whatever their value for economic theory and history may be.
65. "And as soon as one gives up the conception of a freely established monetary price for goods of a higher order, rational production becomes completely impossible. Every step that takes us away from private ownership of the means of production also takes us away from rational economics....

    "The administration [of the socialist state] may know exactly what goods are most urgently needed. But in so doing, it has only found what is, in fact, but one of the two necessary prerequisites for economic calculation. In the nature of the case, however, it must dispense with the other—the valuation of the means of production....

    "Where there is no free market there is no pricing mechanism; without a pricing mechanism, there is no economic calculation....

    "Exchange relations between production goods can only be established on the basis of private ownership of the means of production" (Mises, "Economic Calculation," pp. 104–11).
66. *Ibid.*, p. 109.
67. Bergson, "Socialist Economics," pp. 445–46.
68. Mises, *Human Action,* p. 710.
69. Bergson, "Socialist Economics," p. 446.
70. *Ibid.*, p. 447.
71. That is, given the highly restrictive meaning that is being attached to the phrases "economic theory" and "practicability in principle," such were not in dispute by Mises or Hayek at any stage of the debate. Putting the argument in terms of "relative efficiency" implicitly understates the seriousness of the calculation problem.
72. Bergson, "Market Socialism Revisited," p. 657.
73. Bergson, "Socialist Economics," p. 435.
74. Bergson, "Market Socialism Revisited," p. 658.
75. Ward, *The Socialist Economy.*
76. *Ibid.*, p. 12.
77. *Ibid.*, p. 14.
78. *Ibid.*, pp. 14–15.
79. *Ibid.*, p. 17.
80. Enrico Barone, "The Ministry of Production in the Collectivist State" (1908), reprinted in Hayek, *Collectivist Economic Planning.*
81. Ward, *The Socialist Economy,* p. 18.
82. *Ibid.*, p. 19.
83. *Ibid.*, pp. 21–22.
84. Hayek, "The Competitive 'Solution.'"
85. Ward's interpretation of Mises is in some respects better than the standard account. The standard account would view Barone's argument as a refutation of Mises' calculation argument, while Ward would view Barone's argument as an earlier and more systematic version of Mises' challenge. Both, however, see Mises as dealing with static equilibrium, in the one case denying and in the other case repeating Barone's formal argument. In our interpretation Mises' argument is consistent with, but not limited to Barone's.
86. Ward, *The Socialist Economy,* p. 22.
87. *Ibid.*, p. 25.
88. The distinction between insurable risk, to which can be assigned a definite cost, and "true" uncertainty will be discussed in the section on Knight.
89. In a number of places Dobb (see his "Economic Theory and the Problems of a Socialist Economy," "Saving and Investment in a Socialist Economy," *An Essay on Economic Growth,* and *Welfare Economics and the Economics of Socialism*) develops a critique of the manner in which choices with respect to the future are made under the capitalist mode

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of production. He contends that such decisions are made irrationally (in particular, shortsightedly) and that they could be rationalized under socialism by consciously planning the rate of new investment. In contrast the Austrians have argued that a spontaneously generated rate of investment, determined by the voluntary consumption/savings ratios of individuals in the market, is more rational than attempts to interfere with it have been. The Austrian business cycle theory, for example, concerns exactly this view, arguing that the policy of credit expansion to manipulate the interest rate in fact introduces the very coordination problems that Dobb believes are inherent to capitalism.

90. Ward, *The Socialist Economy,* p. 26.
91. That is, a centralized socialist economy which lacks a rivalrous market process would also lack an equilibrating tendency. But if decentralization of price decisions is permitted, then the question becomes whether the equilibrating tendency is obstructed by interventionist government policy or allowed to freely influence the price system. Mises formulated different arguments against this "interventionist" system, but the close relationship of these arguments to the calculation argument has been lucidly described by Kirzner. See Israel M. Kirzner, "The Perils of Regulation: A Market-Process Approach," *Law and Economics Center: Occasional Paper* (Coral Gables, Fla.: University of Miami School of Law, 1978).
92. Ward, *The Socialist Economy,* p. 24.
93. See, for example, Mises, *Socialism: An Economic and Sociological Analysis,* p. 140 (added to the 1932 edition) on risk, and *ibid.,* p. 117 on information.
94. Ward, *The Socialist Economy,* p. 25.
95. *Ibid.*, p. 24.
96. *Ibid.*, p. 25.
97. Hayek, "The Present State of the Debate"; and *idem,* "The Competitive 'Solution.'"
98. Ward, *The Socialist Economy,* p. 28.
99. Lerner, *Economics of Control,* p. 3.
100. Ward, *The Socialist Economy,* p. 29.
101. Lerner, *Economics of Control,* p. viii. Ward concurs with our interpretation that Lerner is essentially arguing in static terms, although at times Lerner himself is ambiguous on this. See, for example, Lerner, "Statics and Dynamics in Socialist Economics."
102. See Ward, *The Socialist Economy,* pp. 37, 70, 73.
103. *Ibid.*, p. 30.
104. Ward specifically refers to Debreu, *Theory of Value* (New York: Wiley, 1959) in this respect, whose model introduces "time" without uncertainty.
105. A large "price adjustment" literature has been produced, much of it more recent than the survey by Negishi ("The Stability of a Competitive Economy") which Ward cites; but we would argue that this approach has not been successful in advancing economics beyond the constraints of static analysis. Indeed, Ward, in "Organization and Comparative Economics," seems to see the major drawback of this kind of approach when he remarks that "stability analysis is typically very crudely mechanistic in its assumptions."
106. While getting beyond "tâtonnement" processes is the aim of Austrian "market process" analysis, the article by F. Hahn and Negishi, "A Theorem of Non-tâtonnement Stability," *Econometrica* 30 (July 1962), which Ward cites, does little to enlighten this path.
107. Edgeworth was only able to overcome this difficulty by inventing another fiction, "recontracting," which, by permitting contracts to be perfectly revokable, makes genuine contractual exchange relations inexplicable.
108. Ward, *The Socialist Economy,* pp. 32–33.
109. See Montias, "Planning with Material Balances in Soviet-type Economics," *American Economic Review* 49 (December 1959); Malinvaud, "On Decentralization in National Planning"; G. B. Dantzig, *Linear Programming and Extensions* (Princeton: Princeton University Press, 1963).
110. In his *The Socialist Economy,* Ward does make some brief references to mathematical "oversimplifications" of these schemes—e.g., that they are static and usually linear (pp. 58–59)—but he underestimates some other potential difficulties. He claims that the

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"communication between sectors and plan bureau . . . cannot be a bottleneck to extension of the schemes" (p. 61). Such communication "involves at each round sets of numbers that should not exceed n^2 for any one unit, where n is the number of sectors, and is generally much less." (Although Ward speaks here of "sectors," for this to be a workable procedure "n" would have to be the number of separately priced items in the economy, a number which when squared and then multiplied by the number of necessary rounds could constitute a considerable bottleneck for the most advanced communication system.) But if, as seems quite likely, "time prevents completion of the iterations needed to generate an optimum," for the more sophisticated of these schemes "the process can be stopped at an intermediate round and will produce a plan which is consistent and an improvement over the starting feasible plan" (p. 61). With this comment Ward is abandoning the major *raison d'etre* of the auctioneer-type process. If producers are to hold up all economic activity while the linear programming experts compute an equilibrium, only to achieve a "feasible" but non-optimal configuration of prices, why wait for such costly computation in the first place? The nontâtonnement processes of a decentralized market under an appropriate legal system can accomplish this imperfect result without the intervention of planometricians.

111. Lippincott, *On the Economic Theory of Socialism,* p. 12.
112. *Ibid.*, p. 9.
113. This lumping together of the three traditions stemming from the marginalist revolution of the 1870's is common in the literature on the debate. For example, Lerner argued that "a reasonable account of modern economic theory by any one of the three methods of exposition will contain the identical doctrine" ("Statics and Dynamics," p. 54).
114. Lippincott, *On the Economic Theory of Socialism,* p. 6.
115. Heimann takes this misinterpretation of Mises to an extreme when he refers to Mises as the theorist "who more than any other economist regards laissez-faire as the system of equilibrium." (Heimann, *History of Economic Doctrines: An Introduction to Economic Theory* [New York: Oxford University Press, 1945]). On the contrary, we contend that Mises was less concerned than almost any other economist with static equilibrium and repeatedly denied that *any* system could *ever* be in equilibrium.
116. Lippincott, *On the Economic Theory of Socialism,* p. 7.
117. *Ibid.*, p. 13.
118. *Ibid.*, p. 17.
119. *Ibid.*, p. 24.
120. Alan Sweezy, "The Economist in a Socialist Economy," in *Explorations in Economics: Notes and Essays Contributed in Honor of F. W. Taussig* (London: McGraw-Hill, 1936), p. 424.
121. *Ibid.*, p. 423.
122. *Ibid.*, pp. 424–25.
123. *Ibid.*, p. 425.
124. Hayek, "The Competitive 'Solution,'" p. 196.
125. Sweezy, *Explorations in Economics,* p. 432.
126. *Ibid.*, pp. 428–29.
127. *Ibid.*, p. 432.
128. Dobb, *Welfare Economics and the Economics of Socialism,* p. 183: "There can remain scarcely any doubt that the von Mises objection in the form in which he stated it cannot be sustained."
129. *Ibid.*, pp. 184, 203–207. Dobb's interpretation of the debate is fully consistent with the standard account, as illustrated by this statement: "The debate . . . was concerned essentially with positions of equilibrium, and with the choice of one among many possible equilibrium positions as the optimum. As such it was conducted in terms of the theory of static equilibrium" (*On Economic Theory and Socialism,* p. 74).
130. Dobb, "Economists and the Economics of Socialism" (1939), reprinted in *ibid.*, p. 242.
131. *Ibid.*
132. Lerner, "Economic Theory and Socialist Economy," p. 58.

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133. Dobb frequently cites, rather uncritically, Soviet growth statistics to support his argument, but besides the point that these growth rates are not as impressive as the Soviet press likes to pretend, even if they were they would prove nothing. The question is how impressive could that economy have been—in terms of the real standard of living of the people—if it had not forced a great deal of productive activity to ignore considerations of microeconomic efficiency.
134. Heimann, *History of Economic Doctrines,* p. 208.
135. Frank H. Knight, "The Place of Marginal Economics in a Collectivist System," *American Economic Review* 26, Supplement (March 1936), p. 255.
136. See Stigler's introduction to the 1971 edition of Knight, *Risk, Uncertainty and Profit* (1921; Chicago: University of Chicago Press, 1971), p. xiv.
137. See Kirzner, *Perception, Opportunity and Profit.* See also the papers by Jack High, "Disequilibrium Economics: Survey and Analyses" (preliminary draft, economics diss., U.C.L.A.); Mario J. Rizzo, "Knight's Theory of Uncertainty: A Reconsideration" (Paper delivered to the American Economic Association, Chicago, August 1978); and Lawrence H. White, "Entrepreneurial Price Adjustment" (Paper delivered to the Southern Economic Association, Washington, D.C., November 1978).
138. Both Shackle, in *Epistemics and Economics,* and Kirzner, in *Competition and Entrepreneurship,* two of the most significant "Austrian" contributions in the 1970's, make this their main point in criticism of neoclassical choice theory.
139. Knight, *Risk, Uncertainty and Profit,* p. 30.
140. Knight, "The Place of Marginal Economics," p. 264.
141. Knight, "'What is Truth' in Economics?" (1940), reprinted in Knight, *On the History and Method of Economics: Selected Essays* (Chicago: University of Chicago Press, 1956).
142. Knight, "The Place of Marginal Economics," p. 263.
143. Knight, "Statics and Dynamics: Some Queries Regarding the Mechanical Analogy in Economics" (1930), reprinted in Knight, *On the History,* p. 187. Knight's wording "process in equilibrium" is misleading here, since the whole point is that the process is in disequilibrium, as the rest of the quotation indicates.
144. Knight, "Socialism: The Nature of the Problem," *Ethics* 50 (April 1940): 258.
145. *Ibid.*, p. 285.

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War Communism to NEP: The Road from Serfdom

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> The collapse of the productive forces surpassed anything of the kind that history had ever seen. The country, and the government with it, were at the very edge of the abyss.
>
> Leon Trotsky on war communism[1]

Introduction

In March 1921, V. I. Lenin, ruler of revolutionary Russia, stood before the Tenth Congress of the Bolshevik Party and dramatically admitted that something had gone awry with the Revolution. The new policy he unveiled that day admitted not only that the Bolsheviks had failed to ignite a world-wide socialist takeover, but that the revolution they did ignite had brought Russia to the "very edge of the abyss."

Four and a half years of "war communism"—the attempted instantaneous obliteration of the market economy—had brought only starvation, death, and destruction. The Bolshevik hold on the nation was tenuous. Something drastic had to be done. What Lenin chose to do is a fascinating and instructive historical episode.

War Communism

The period from 1918 to 1921—the period of war communism—may be described as a leap into socialism. Whereas Marx had predicted that capitalism would mature into a proletarian revolt and then a socialist dictatorship, the architects of the new Russia sought to skip key Marxian historical steps and proceed directly to the workers' state. To do this Lenin had to depart radically from orthodox Marxist strategy.

> Lenin had originally accepted Plekhanov's deterministic interpretation of classical Marxism....But by 1900, Lenin recognized that the working class movement, isolated from the leadership of revolutionary Marxists, would be irredeemably "petit bourgeois." By the end of 1901 Lenin insisted that a revolution required the intercession of a critical revolutionary elite....Nowhere did classical Marxism explicitly enter-

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> tain the conviction that a revolutionary party and a revolutionary leadership was either the necessary or sufficient condition of the revolution.[2]

If the small Russian proletariat and a large number of peasantry were not ready to inaugurate socialism spontaneously (as envisioned by Marx), then Lenin and his professional cadre would do it for them. The result was war communism.

Much has been said about this period, but perhaps the most succinct description of its meaning was provided by economist Jack Hirshleifer. He called war communism "the most extreme effort in modern times to do away with the system of private property and voluntary exchange." In the eyes of the Bolsheviks the market was the most "bourgeois" institution and therefore most deserving of immediate destruction. As leading Bolshevik theoretician Nikolai Bukharin wrote in *The ABC of Communism*, "We see, therefore, that the primary characteristic of the capitalist system is a commodity economy; that is, an economy which produces for the market."[3] In another book, *The Economics of the Transition Period*, Bukharin elaborated: "Indeed, as soon as we deal with an organized national economy, all the basic 'problems' of political economy, such as price, value, profit, etc., simply disappear."[4]

In one fell swoop the market was declared illegal. Private trade, the hiring of labor, leasing of land, and all private enterprise and ownership were abolished, at least in theory, and subject to punishment by the state. Property was confiscated from the upper classes. Businesses and factories were nationalized. Surplus crops produced by the peasants were taken by the government to support the Bolshevik civil-war forces and workers in the towns. Labor was conscripted and organized militarily. Consumer goods were rationed at artificially low prices and later at no price at all. Unsurprisingly, special treatment was accorded those with power and influence.

The results were catastrophic. Industrial production by 1920 was 20 percent of the pre-war volume. Gross agricultural output fell from more than 69 million tons in the period 1909–1913 to less than 31 million in 1921. Sown area dropped from over 224 million acres in the period 1909–1913 to less than 158 million in 1921. From 1917 to 1922 the population declined by 16 million, not counting war deaths and emigration. Eight million persons left the towns for the villages from 1918 to 1920. In Moscow and Petrograd, the population declined 58.2 percent.[5]

With industrial production at a near standstill, the towns had little to trade with the peasants for food. With no incentive for the peasants to produce a food surplus, the government turned to confiscation, which further discouraged agricultural production. The peasants resisted the harsh government measures.

> The peasant was required to deliver everything in excess of his own and his family's needs. Naked requisition from so-called kulaks [the more

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> prosperous peasantry] of arbitrarily determined surpluses provoked the two traditional replies of the peasant: the short-term reply of concealment of stocks and the long-term reply of refusal to sow more land than was necessary to feed his own family.[6]

While the Bolshevik assault on the market economy was comprehensive and brutal, it would be a mistake to think it was fully successful. The market impulse dies hard and there was an extensive black market for consumer goods. It has been suggested that the black market and pre-war production are what carried the Russians through the civil war and delayed the total collapse.

> In 1920, the Reds faced an internal situation verging on catastrophe. Hunger and disease were widespread, and industry and trade were at a virtual standstill.[7]

> The attempt to run an entire economy like an army, extending to the requisition of crops, the conscription of labor, and the abandonment of money accounts failed utterly.[8]

What went wrong? One of the architects of war communism, Leon Trotsky, later provided a candid answer:

> The Soviet government hoped and strove to develop these methods of regimentation directly into a system of planned economy in distribution as well as production. In other words, from "war communism" it hoped gradually, but without destroying the system, to arrive at a genuine communism.... Reality however came into increasing conflict with the program of war communism.[9]

Trotsky's blunt admission is highly accurate. Several aspects of reality stood in the Bolsheviks' way. It was at best naive for them to think the peasants would go on producing under these circumstances. (Indeed, tax rebellion is one of the oldest human endeavors.) Furthermore, as paradoxical as it may seem, a centrally directed economy is the least fit for organizing production. In other words, the "planned economy" cannot plan.

This was the insight of "Austrian" economist Ludwig von Mises in his pioneering work of the 1920's. Mises showed that without free exchange in capital and consumer goods, there is no market; that without a market there are no prices; and that without prices there can be no economic calculation. Socialism must bring economic chaos because it cannot rationally calculate costs and income and thereby plan productive activities. Mises wrote:

> Without calculation, economic activity is impossible. Since under Socialism economic calculation is impossible, under Socialism there can be no economic activity in our sense of the word....All economic change, therefore, would involve operations the value of which could neither be predicted beforehand nor ascertained after they had taken place. Everything would be a leap in the dark. Socialism is the renunciation of rational economy.[10]

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The measures and results of war communism led social historian Ralph Raico to this view of the Russian Revolution:

> What we have with Trotsky and his comrades in the Great October Revolution is the spectacle of a few literary-philosophical intellectuals seizing power in a great country with the aim of overturning the whole economic system—*but without the slightest idea of how an economic system works.*[11] (His emphasis)

One final point: Whether war communism was a deliberate part of the Bolshevik program or a temporary expedient prompted by the civil-war emergency has been a matter of some controversy. However, statements by Lenin and others during and after this period show explicitly that war communism was the deliberate aim of the revolution and unrelated to the civil war. Lenin's apologies for this "mistake" in attempting the quick route to socialism would have been unnecessary had war communism been adopted as an emergency measure.[12]

If war communism is regarded as a shortcut to Marxian socialism, the ensuing period becomes even more instructive.

The New Economic Policy

In 1921, an extremely poor harvest struck Russia. The civil war had ended in the spring, but the effects of war communism showed no signs of abating. Looking back, Lenin wrote, "On the economic front, in our attempt to pass over to Communism, we had suffered, by the spring of 1921, a more serious defeat than any previously inflicted on us."[13]

The peasants, no longer fearing the return of the old landowners, turned their full attention to their other enemy, the Bolshevik state. Peasant uprisings ignited spontaneously throughout the country beginning in the spring of 1920, protesting shortages and government centralization. The climax came in March 1921, with the armed rebellion at the Kronstadt naval base, one-time Bolshevik stronghold. The sailors at Kronstadt sympathized with the rebellious civilians and formally called for an end to Soviet tyranny. The sailors' platform demanded freedom of speech, press, and assembly for workers, peasants, and political parties; release of political prisoners; and abolition of special privilege for Communist Party officials. "The platform promised the peasants full rights to do as they liked with their land, and advocated the ending of discrimination in food rationing."[14]

Government efforts failed to end the rebellion peacefully, and the sailors set up a Provisional Revolutionary Committee on March 2, 1921. On March 18, a force directed by Trotsky attacked the sailors' fortress and crushed the rebels. Some 15,000 participants eventually were killed without trial, but the incident led to essential changes in the Soviet Union, specifically to the New Economic Policy.

If war communism was a leap toward socialism, the NEP was half a leap

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toward capitalism. At the Tenth Party Congress in March 1921, Lenin outlined a program intended to undo the conditions that had set the peasants against the regime, pushed the nation to the verge of destruction, and weakened the Bolshevik grip. As Carr put it,

> The antidote [to war communism], familiarly known as NEP, was... a series of measures not conceived at a single stroke but growing gradually out of one another. It began, by striking at the point of greatest danger, as an agricultural policy to increase the supply of food by offering fresh inducements to the peasant; it developed into a commercial policy for the promotion of trade and exchange, involving a financial policy for a state currency; and finally, reaching the profoundest evil of all, it became an industrial policy to bring about that increase in industrial productivity which was a condition of the building up of a socialist order. The essential feature of NEP was the *negation or reversal of the policies of war communism.*[15] (Emphasis added)

The reform was comprehensive. The first and major change was the elimination of grain requisitioning and substitution of a proportional tax, first in kind, then in currency, levied on the peasants individually. The peasants were now free to keep a portion of their surplus production and trade it in the markets that developed as a result. The inducement to produce was a tonic that had immediate effects. The harvest of 1922 was most favorable, and agricultural production returned to the pre-war level by 1925.

Besides the change in the tax, other measures were enacted to facilitate the recovery of free trade. When collectivization of farming met resistance, private landholdings were allowed. Peasants were free to cultivate the land as they wished and were granted security of tenure. At first there was only surreptitious leasing of land and hiring of labor, but by the end of 1922 this was permitted by the new agrarian code. Compulsory labor was abolished; wages were linked to productivity. Workers could be fired by their employers.

One of the most significant developments was the spontaneous appearance of a class of brokers—called nepmen—to coordinate the buying and selling of peasant surpluses. This entrepreneurial element is one of the defining features of a market economy.

Central planning was abandoned and money accounts were restored. In 1922 and 1923 private trade accounted for 90 percent of distribution.[16] Nationalization of industry ceased. While some enterprises were nominally owned by the state, they were leased to individuals and operated privately. Government subsidies were stopped, and enterprises were expected to make their own way purely by buying and selling in the market. Heavy industry, which represented a minority of enterprises, was required to give priority to the state, but permission to sell in the free market was frequently given. Combinations of enterprises, called trusts, were formed during the period

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and were permitted to make profits. By 1924, industrial production returned to almost half the 1913 level.[17]

Disillusion with a moneyless economy persuaded the government of the importance of money, banking, and capitalist accounting principles. All were restored under the NEP. The government even introduced a gold ruble. The demand for money, which had plummeted under war communism because of the severe shortages and fear of repudiation, soon rose substantially as consumer goods became available.

The recovery bordered on the miraculous. Both town and village benefited from the increased supplies of goods. "The reanimating influence of NEP spread over every part of the economy. . . ."[18] At the fourth Congress of the Comintern, November 1922, Lenin boasted,

> The peasant risings which formerly, before 1921, were, so to speak, a feature of the general Russian picture, have almost completely disappeared. The peasantry is satisfied with its present position. . . .This has been achieved in the course of a single year.[19]

Introduction of the NEP was necessarily risky in a land ruled by doctrinaire socialists. Lenin, the pragmatist, realized that to cleave to orthodoxy would have meant rebellion by the peasants and an end to the regime. He bluntly called the NEP a "retreat" and a "defeat"[20] that would be made up once the country was economically healthy. He preferred concessions to the peasants rather than destruction of his life's work, and he was willing to go to great lengths to placate them. In 1921 he said,

> We are Bolsheviks, not Communists. We are for the Bolsheviks because they drove out the landowners, but we are not for the Communists because they are against individual holdings.[21]

Lenin justified the NEP on grounds that "state capitalism" was the last stage of capitalism before socialism evolved. One historian writes:

> Lenin used the term "state capitalism" because he was counting on the cooperation of Russian capitalism and, even more so, on large foreign capitalist interests; he thought that Russia needed a long period of capitalist development in order to assimilate organization methods and technical expertise, and to acquire the capital and intellectual abilities that the worker's state did not yet possess. . . .According to Lenin, the principle enemy of the state was no longer big capital, but the unruly, fragmented petit bourgeois sector that eluded all state planning and control. Only big capital possessed the qualities that were useful to progress: its ability to organize on a large scale, its tendency to plan and its sense of discipline.[22]

When cooperation of big capital couldn't be attracted, Lenin doubled his efforts to win over the peasants. Collectivization of agriculture, which never found favor with the peasantry, was dropped in an attempt to placate the poor and middle-class peasants. (Programs to create class conflicts

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Stalin's victory doomed the prospects for an expansion of the small measure of freedom that existed. On December 27, 1927, the 15th All-Union Congress of the Communist Party, now in Stalin's hands, condemned all deviation from the party line and adopted "measures that signified the end of the New Economic Policy and the beginning of the First Five-Year Plan."[26]

The plan included an all-out effort to collectivize farming, new restrictions on the citizenry, and the stripping of the kulaks' rights. Just before the plan's introduction, the kulaks resisted demands that they deliver grain at low, state-fixed prices. In 1927, state acquisition of grain fell two million tons short of the minimum required. When the Central Committee set local party members on the peasants to extract the grain, the peasants resisted. Where the pragmatic Lenin may have searched for new incentives for the peasants, Stalin cracked down.

The relative peace of the NEP was replaced by the violence of Stalinism, under which 5 million kulaks and their families disappeared. Land and industry were brutally collectivized, and central planning was imposed on the economy. However, having learned at least a partial lesson from the severe failure of the 1918–1921 period, Stalin never even contemplated a return to the moneyless economy of war communism.

NOTES

1. Quoted in Ralph Raico, "Trotsky: The Ignorance and the Evil," *Libertarian Review* 8, no. 2 (March 1979): 39.
2. A. James Gregor, *The Fascist Persuasion in Radical Politics* (Princeton: Princeton University Press, 1974), pp. 105–106.
3. Quoted in Paul Craig Roberts, *Alienation and the Soviet Economy* (Albuquerque, N.M.: University of New Mexico Press, 1971), p. 13.
4. *Ibid.*, p. 13.
5. Jack Hirshleifer, *Disaster and Recovery: A Historical Review* (Santa Monica, Calif.: The RAND Corporation, 1963), pp. 19, 23, 28.
6. Edward Hallett Carr, *The Bolshevik Revolution, 1917–1923,* vol. 2 (London: Macmillan, 1952), p. 150.
7. Donald Treadgold, *Twentieth Century Russia* (Chicago: Rand McNally, 1972), p. 188.
8. Hirshleifer, *Disaster and Recovery*, p. vi.
9. Raico, "Trotsky," p. 40.
10. Ludwig von Mises, *Socialism: An Economic and Sociological Analysis* (London: Jonathan Cape, 1936), pp. 21–22.
11. Raico, "Trotsky," p. 40.
12. Roberts, *Alienation*, pp. 20–47.
13. Quoted in Hirshleifer, *Disaster and Recovery*, p. 19.
14. Basil Dmytryshyn, *The USSR: A Concise History* (New York: Charles Scribner's Sons, 1978), p. 117.
15. Carr, *The Bolshevik Revolution*, p. 272.
16. Hirshleifer, *Disaster and Recovery*, p. 28.
17. *Ibid.*, p. 26.
18. Carr, *The Bolshevik Revolution*, p. 295.
19. *Ibid.*, p. 295.

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among the peasants had proved futile.) The much reviled kulaks—the better-off, capitalist-oriented peasants—remained objects of suspicion and envy, but their value in revitalizing the economy was undeniable.

No doubt Lenin's complimentary references to capitalism were disconcerting to some. The NEP, while regarded as important economically, was feared politically.

> The NEP was like a mine that had been placed under the still insecure structure of the new regime. Whether he would have admitted it or not in public, Lenin was no less concerned than other militants at the prospects of such a threat.[23]

> At first, every section of opinion within the Party accepted this solution as the only possible one, but many soon came to regard it as a betrayal, an alliance contrary to nature. In any case, the Party was worried, and not without reason, for now the illusions created by "war communism" were shattered: the peasant market and the capitalist spirit would not fail to penetrate every sector of Soviet life and act as an element of corruption and dissolution, affecting the state and even the Party. Many would have endorsed the view of Rosa Luxemburg (expressed in 1918): "Leninist agrarian reform has created a new and powerful layer of popular enemies of socialism on the countryside, enemies of whose reistance will be much more dangerous and stubborn than that of the noble large landowners."[24]

Dmytryshyn points out two objections to the NEP made by orthodox socialists. First, introduction of market practices sacrificed central planning to the well-being of the peasants, who were never sympathetic to socialism. (They were grateful that the noble landowners had been run off the land, but now they wanted to be left alone to cultivate it.) Second, a prosperous peasantry and small-entrepreneur class would ultimately change the political "superstructure" by reviving the spirit of capitalism.[25]

Despite the undeniable improvement in living standards, party officials feared things were slipping beyond their control. The NEP became a central point of controversy in the three-way rivalry that followed Lenin's death in 1924. Trotsky, leading the left faction, opposed the NEP, believing that world-wide socialist revolution was needed to save socialism in Russia. (Trotsky may have been nostalgic for the forced labor and regimentation of the previous period.)

The right faction, headed by Bukharin, who was now sympathetic to a market orientation, believed the NEP should continue because world-wide socialism was not in the offing.

Finally, the center, led by Stalin, agreed that world revolution was not near, but held that socialism could be established in Russia nonetheless. Stalin, originally closer to Bukharin, managed to eliminate both Trotsky and Bukharin and eventually consolidated his power and took over the government.

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20. *Ibid.*, p. 276.
21. *Ibid.*, p. 165, n. 4.
22. Moshe Lewin, *Lenin's Last Struggle* (New York: Random House, 1968), p. 2.
23. *Ibid.*, p. 23.
24. *Ibid.*, p. 22.
25. Dmytryshyn, *The USSR*, p. 121.
26. Nicholas V. Riasanovsky, *A History of Russia* (London: Oxford University Press, 1968), p. 544.

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The Failure of Bolshevism and Its Aftermath

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Even after the bitter defeat of War Communism, Lenin never doubted that socialism entailed the abolition of trade and money. The Soviet doctrine of "socialist commodities" did not enter the picture until the 1950's. Compelled to preside over the encouragement of the market, Lenin continues to assert: "Exchange is freedom of trade; it is capitalism."[1] He wrings his hands, complaining that "capitalism must grow out of this soil of free trading."[2]

As he explains the need to permit the growth of trade, he continually has to remark upon the unheard-of novelty of socialists doing any such thing. "Communism and trade?! It sounds strange. The two seem to be unconnected, incongruous, poles apart." Like many Marxists he believes that capitalism requires a gold standard. He naturally draws the conclusion that compromise with capitalism requires acceptance of gold. "When we are victorious on a world scale I think we shall use gold for the purpose of building public lavatories in the streets of some of the largest cities of the world." But "for another decade or two" it is necessary to work slowly towards that goal. "Meanwhile, we must save the gold in the R.S.F.S.R., sell it at the highest price, buy goods with it at the lowest price. When you live among wolves, you must howl like a wolf...." In due course, however, all the wolves will be exterminated.[3]

It is often claimed that the retreat to the "New Economic Policy" (NEP) was necessary because the socialist revolution in the West failed to materialize. Undeniably, the Bolsheviks banked on imminent revolutions elsewhere. But once they had taken power, it would have been intolerable to conduct practical administration on the assumption that the West would come to their rescue the following day. What were they to do in the meantime? Under Lenin's direction they decided unequivocally that they would proceed at once to construct a socialist economy. Lenin soon acknowledged that the Western revolutions might be awaited for several years, but he never suggested that socialist construction should therefore be postponed.

The fact that the Bolsheviks were wrong in expecting a German revolution should be placed in its context: the Bolsheviks were wrong in all their expectations. Everything turned out just as the anti-Bolshevik Marxists had predicted, only to be ridiculed, vilified, and in due course,

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shot. The crucial question is how the Bolsheviks would respond to the occurrence of that which they had violently denied could occur. Would they, perhaps, admit that the *coup* had been a sorry blunder, that they had made a complete mess of things, that the workers had not benefited in the slightest degree from their actions, and that they should abdicate all power at once? This kind of humility is rare among politicians. But if the Bolsheviks refused to accept that the *coup* had been at best futile, the heresy of "socialism in one country" (as yet unformulated) was implicit in everything they did.

And if revolutionary socialists had taken power in Germany, how could they have saved communism in Russia? Of course, the Marxists did not realize that central planning in Western Europe would necessarily bring about even greater collapse and slaughter than it did in backward Russia. But suppose that a successful German socialist revolution led to a miraculous (say, an immediate five-fold) increase in German industrial production. The collapse in Russia was so bad that the Germans could have helped significantly only by reducing their own living standards to send massive handouts to Russia, and even this would have been but a temporary palliative.[4]

One of the main reasons why it had been assumed socialism could not survive in a single country was the likelihood that the surrounding bourgeois powers would overthrow it. But Lenin was quick to see that the war, and then the war-weariness of the Western powers, forbade massive intervention. He therefore argued that the Bolsheviks could take advantage of the war to "advance and consolidate the socialist revolution."[5] He predicted: "our success in reconstructing the social economy is inevitable, provided we are not crushed by military force."[6] The Bolsheviks had always been prepared for the possibility that they would go down in a blaze of glory, like the Paris Commune. They were totally unprepared for the possibility that the central direction of industry would prove rather difficult, let alone that it would be beyond their capacity.

The Failure of Bolshevism

Judged by its announced goals, Bolshevism failed. The question arises whether its failure did not simply prove the traditional Marxists correct: Russia was "not yet ripe" for socialism. It is not self-evident, however, that more advanced industry would be "more ripe." If any part of the War Communism catastrophe was due to the inability of the planners to allocate factors appropriately in the absence of market prices, that would suggest that a more advanced industry would be harder to communize.

Peasant resistance to requisitions played a large part in the fiasco, but according to Brutzkus, whose early account has never been refuted, the collapse of production was greatest in large-scale industry.[7] First and fore-

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most, War Communism was a system of administering industry. Each enterprise put its products at the disposal of a central board, and applied to the board for its supplies of means of production. Since there was no price system, the board had no sensible way to allocate means of production to enterprises. An enterprise can choose its assortment of inputs only when these are priced. If each input is acquired by a sort of lottery, dependent on filling in a form and then waiting to see who gets priority, it is unlikely that the assortment which is delivered will be of much use, though it may contain items which would be highly productive in combination with others which have been allocated elsewhere. "As the means of production are complementary the whole of industry was in this way gradually paralyzed, although the country still possessed considerable stocks of unused production goods."[8]

NEP was seen as a temporary retreat, but there was no agreement as to how long it would last. Large-scale industry remained in the hands of the state. Lenin described these nationalized undertakings as "socialist," and saw the immediate future as a continuous struggle between socialism and capitalism. Perhaps he saw NEP lasting from ten to twenty years.[9] But this was highly improbable. The logic of the situation drew the government towards further attempts at central planning. Even governments with no ideology of market-abolition find themselves, once they engage in extensive intervention, itching to go further, to poke their thumbs into more and more pies. Here was a government with despotic powers, committed to the eventual triumph of socialism, defined strictly and explicitly as a natural economy, and smarting from the disgrace of a recent debacle. Even such a government might conceivably have come to terms with reality, except that War Communism had already been covered in legend and falsification, as even its name indicates. No honest criticism of War Communism could be made. Russia was already a totalitarian society.

The government intervened to fix more and more prices below market levels. Shortages resulted. The government responded to the shortages by decreeing further price cuts, with worse shortages resulting. In default of abandoning these price controls, the government "had" to step in to administer the distribution of vital goods. At the same time the Communist Party sanctioned numerous "plans," for large-scale industry, foreign trade, transport and so forth, and wherever this occurs it is only reasonable to demand that all the plans be harmonized, which is tantamount to having a single general plan. The first outline of such a plan was published in 1925. "Control figures" were issued, based on a methodology which, twenty years later in another country, would be termed "indicative planning." Indicative (toothless) planning, the publication of forecasts, or wishes, in the hope that this will make them materialize, must always give way either to no planning or to attempts at real planning, in which the forecasts or wishes become orders.

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"During the winter of 1927–28 the kulaks [middle-class peasants] seized the Soviet state by the throat,"[10] wrote Ernest Mandel. What actually happened was that the Communist Party government kept cutting the price of foodstuffs. They cut the price of grain by more than 20 percent during 1926–27.[11] The government's ignorance of economic theory did not prevent the peasants from acting in strict conformity with it. They shifted to other crops, sold at higher prices to the remaining private traders, fed grain to livestock, and held back grain in expectation of a rise in the official price. But, in January 1928, the government closed the country markets and reintroduced the compulsory confiscation of War Communism.

War Communism, Mark Two

The first Five-year Plan was sanctioned by the Government in May 1929, but was supposed to operate from October 1928. (Thus was begun the custom of deciding upon the "plan" after the commencement of the planning period.) It was based upon the indicative Control Figures which had been drawn up earlier, mainly by non-CP economists, but for the 1929–30 Control Figures, the "bourgeois" experts were replaced by Communists. According to Brutzkus:

> In 1930 the following views were dominant in economic literature.... the N.E.P. system had been overcome, the Soviet economic system had already reached the stage of complete socialism. Money issues could be made without concern, for money was now nothing but an accounting symbol which one would soon be able to dispense with. One must accustom oneself to disposing of goods in kind. If, however, the Soviet economy would need a measure of value, then not money but the labour day was appropriate to socialism.
>
> The economic ideology of the period of War-communism lived again.[12]

This was not surprising, since that was nothing more nor less than the economic ideology of Marxism and Bolshevism. The Five-year Plan was still based on monetary reckoning, but the Communists had not fully digested what this implied. For example, there was a state bank, but it supplied funds indiscriminately for all projects sanctioned by the plan. It is idle simply to decree the use of money, credit and banks. To be of any use, "money" must *function as money.*

Thus there occurred "a partial relapse of the economic plan, originally designed on a money basis, into a condition analogous to that of natural socialism; yet the unsoundness of this system had already been proved by experience." According to Brutzkus, by the beginning of 1931, "the Soviet economic system was on the brink of general disintegration."[13] Collapse and famine once more stared the Communists in the face.

But by 1931 Stalin was in command. During 1931 he moved swiftly. The

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credit system was brought into line with capitalist practice. Direct, horizontal relations between buyers and sellers were renewed, instead of the solely vertical relations necessitated by genuine central planning. All profits had previously been centralized with the treasury, but now half were to be left with the individual enterprises. (Already, in 1929, it had been accepted that enterprises were to be the economy's basic units, one-man managed, endowed with a legal personality, and conducting their accounting on the basis of monetary profit-and-loss.) Rations in kind, which still prevailed, were completely phased out in favor of money wages, and all talk of equalizing wages was henceforth abused as petty-bourgeois, Trotskyist, anti-Marxist and anti-Leninist. Piece wages (described by Marx as "the form of wages most in harmony with the capitalist mode of production"[14]) were made general. The term "socialist distribution" was dropped in favor of "Soviet trade." "Control by the ruble" became the watchword. The Russian system developed the essential identity it retains to this day: commodity production dressed up as central planning.

War Communism, Mark Three

Nearly 43 years after the abandonment of the original War Communism, the Cuban Industries Minister, Ernesto Guevara, produced an article "On the Budgetary System of Finance,"[15] whose ideas soon came to dominate Cuban government thinking. Guevara comments on Marx's conception of the transition to communism, pointing out in passing that Marx did not envisage any role for money even in the earliest stages. Guevara recalls Lenin's "retreat" from War Communism to NEP, and states that it was "a tactic closely tied to the historical situation of the country," i.e. Russia in 1921, and therefore without "universal validity." Because of the level of development of administrative technique in the Cuba of 1964, there is no need for Cuba to repeat Lenin's retreat.[16] Guevara's "budgetary system," already being implemented when he wrote, is a conscious imitation of War Communism. Enterprises are no more than technical and administrative units, with no independent legal existence and no funds of their own. They are all "part of the single great enterprise that is the state." Central planning displaces the market's hated "law of value"; moral rather than material incentives are to be used wherever practicable, to prepare people for the end of money, and "prices" must be assigned to products on the basis of labor-time.[17]

Castro and his friends were committed Marxian communists before the capture of power.[18] After a brief period of "moderate reform," during which they eliminated their opponents, the new rulers carried through a rapid program of nationalization and centralization. Within a few years, Guevara was putting forward impassioned yet fairly elaborate pleas for the rapid transition to communism, and he was soon followed by Castro.[19]

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All the usual arguments were trotted out: central planning would necessarily be far more efficient than the blind anarchy of the market; communism would be able to save on all the office work involved in charging and collecting money; people would increase output prodigiously now that they were no longer exploited. There was a lot of tinkering with "socialist competition" and "voluntary" additional labor, and many services were supplied to everyone free. The Cuban rulers were aware that they were attempting something that had failed dismally in Russia, but they pointed out that conditions in Cuba were far more propitious. Surely no one could imagine that an internal market was necessary to coordinate production in this small island, which had been greatly centralized already by the imperialist exploiters. There was no debilitating civil war, and Cuba was far from isolated. Staggering sums of economic aid were poured by the Soviet Union into Cuba, already one of the richest countries (per head) in Latin America. An army of helpful technicians and planning experts arrived from Czechoslovakia and other parts of the Russian empire, to be joined by numerous Marxist academics from Western countries, all eager to offer their most up-to-date thoughts on the transition to communism.

Despite these favorable portents, the outcome was disastrous. Cuba's "crash" industrialization program really did crash, with enormous investments wasted because, in the absence of profitability, they could not be coordinated properly.[20] Castro then swung wildly from industry to agriculture. The whole of Cuban society was geared, by the most intensive militarization and indoctrination (there is only one newspaper in Cuba and it contains no news), to the great "Ten Million Ton Sugar Harvest" of 1970, the failure of which could hardly have been more abject.[21] Castro has now permitted the re-emergence of a limited market, and Cuba seems to be becoming more of a conventional Soviet-style state.

Both Lenin and Castro set out to abolish the market, proclaiming that it would be a simple task. Both Lenin and Castro eliminated anyone who said the task was impossible. When things turned out exactly as those eliminated had predicted, both Lenin and Castro admitted frankly that they had made some mistakes, and this admission caused their followers to swoon with admiration at such eviscerating self-criticism.

There will probably be several further War Communisms in less-developed parts of the world.[22] One might suppose that scientific socialists would analyze the experience of previous failures before embarking on their own market-abolition projects, at enormous cost in human life. But "scientific socialism" rests squarely on failure to comprehend the allocative function of the market. Given that failure, it will always be possible for fresh generations of Bolsheviks to find novelties in the world around them, indicating that *this* time conditions are at last ripe for the great leap into communism.

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Does Russia Refute Mises?

It is very commonly asserted that the industrialization of Russia under a centrally-planned, socialist regime is proof in itself of the fallacy of Mises' economic calculation argument. Mises claimed that socialism was impossible. Socialism exists in Russia. Therefore Mises was undoubtedly mistaken.

Four counter-considerations leap to mind:

1. Soviet Russia is not socialist in the sense widely recognized by avowed socialists (including all Marxists) at the time when Mises first presented his argument. Russia retains an internal market and could not do without it.
2. Russia is dependent on the market system in the rest of the world.
3. The Soviet economy is plagued by what the official economists now openly admit to be monstrous irrationalities.
4. It is widely admitted that if Russian society is to advance into the modern world (in technology and living standards), it must progressively abandon its present system in favor of more freedom to the market.

It might be supposed that there is a contradiction in advancing all four of these arguments simultaneously, because the last three seem to accept the designation of Russia as socialist, while the first rejects this designation. Yet they can be reconciled: the degree of central direction is insufficient to qualify as Marxian socialism, but quite sufficient to constitute an insurmountable obstacle to the effective operation of Western-level technology.

That Russia is not socialist in the Marxian sense should by now be clear. It is certainly a system in which commodity production prevails and is being expanded, as the regime's court intellectuals have to admit. There could scarcely be any revision of Marx or Lenin more fundamental than the concept of "socialist commodity production." Neither is money in the Soviet Union confined to the rationing of consumer goods. Commercial dealings have persisted since 1921 (and are now proliferating) between industrial enterprises. Marxism affirms that expansion of the productive forces (capital, skills, technology) leads to the obsolescence of commodity production (the market). Russian experience suggests that the more developed the forces of production, the greater must be the scope allowed to commodity production.

Mises himself put all the weight of his argument on point 2. He accepted Soviet Russia as a specimen of socialism, and observed that the central planners could refer to world market prices in order to perform economic calculation.[23] Russia is chronically dependent upon the Western market.[24] There is no need to fear a world-wide Soviet system, which would be as unviable as a forest of mistletoe.

As to point 3., the aberrations of the Soviet system are by now well known.[25] In the course of his perfunctory dismissal of the Mises case, Bergson makes these curious remarks:

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> If there is no "practicable" basis for rational calculation, the economy presumably would break down....the Soviet planned economy has been operating for thirty years. Whatever else may be said of it, it has not broken down.[26]

These words were written in the forties, so within the previous thirty years the Soviet economy had indeed "broken down" amid "chaos" at least once, in 1921. It came very close to doing so again in 1931. Subsequently, it is true, there was neither chaos nor breakdown, but there *was* continuous "waste on a vast scale."

Point 4. is however now commonly accepted. Unless "economic reform" of a really radical nature can be pushed through, the Russian empire will remain a moribund, backward economy, with no hope of raising the people's living conditions substantially above their present wretched level. And there is little dispute that "economic reform" can mean only less central direction and more market freedom.

The way this is sometimes phrased is that Stalinist central planning was a useful instrument for rapid industrialization, but that it has outgrown itself, and must give way before the transition to a consumer-oriented industry. But the point of production is to serve consumption. Building steel mills, dams and chemical plants is not industrialization in any useful sense if these installations cannot be utilized for satisfying the people's wants.[27] Just as much of British industry now consists of "industrial museums," a net deduction from the welfare of the people, so it has yet to be shown that Russian industry is much more (apart from military applications) than "industrial pyramids." That can be determined only by using this industrial structure to raise the people's living standards or what amounts to the same thing, by seeing which of the existing plants remain profitable upon the introduction of a free (or freer) market.

Is the Soviet Union a Planned Economy?

The basic pattern of Soviet "central planning" emerged from the First Five-year Plan: its distinctive feature is the method of "material balances." Each enterprise is given an instruction from above, to produce a target, usually expressed in some physical magnitude such as weight or quantity of articles, but sometimes formulated in monetary value. For overshooting its target, the enterprise receives financial and other rewards. For failing to reach it, the enterprise is penalized.

As well as attainment of the target, other criteria are enforced, such as quality specifications and reduction of production costs. Each enterprise has its own profit-and-loss acount, and must strive to maximize its profits, some of which it is permitted to retain for its own purposes. But sheer size of output is the main concern of "the plan." The planners' job is apparently

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to draw up, and then communicate, a single plan of national production, in which the physical outputs and inputs of every enterprise are meshed together.

There is no doubt that enterprises receive orders from on high instructing them what to produce, and that in general they try to obey them. This seems to be a clear case of central planning: the planners must somehow conceive of a pattern of operation for the entire economy, translate it into detailed instructions, and see that these are carried out. But things are not as they seem.

One immediately wonders why there is any need for profits or monetary dealings between enterprises. If the plan were all that it seemed, these would be redundant. One also wonders how adjustments are made to take into account over- and under-fulfillment of plans—surely not by the planners being instantly and simultaneously aware of all the technical proportions, stocks of factors and possibilities of substitution for every workshop in the land.

The basic plan documents must be drawn up by people who cannot know what they really mean. These plans have to be formulated in broad categories: so many rivets, so many girders of such-and-such a length. The planners do not know all the various subdivisions, styles and models appropriate to every particular task. The broad aggregates in which they must deal are not very informative about the real interconnections and interactions of one enterprise with another. The absurdity of supposing that genuine planning could be carried on in this way is brilliantly summed up by Michael Polanyi in a striking simile:

> The products are divided into classes and sub-classes. We may see for example Industry and Agriculture as our main divisions. Then Industry may be subdivided into Production of Raw Materials, Finished Products and Industrial Services, while Agriculture may again fall into parts, such as Food Production, Forestry and Raw Materials for Industry. Each of these classes can be subdivided again into sub-classes and this process can be continued until we finally come down to the proposed quantities of individual products, which form the ultimate items of the plan.
>
> At first sight this looks exactly like a true plan, namely like a comprehensive purpose elaborated in detail through successive stages.... But in reality such an alleged plan is but a meaningless summary of an aggregate of plans, dressed up as a single plan. It is as if the manager of a team of chess-players were to find out from each individual player what his next move was going to be and would then sum up the result by saying: "The plan of my team is to advance 45 pawns by one place, move 20 bishops by an average of three places, 15 castles by an average of four places, etc." He could pretend to have a plan for his team, but actually he would be only announcing a nonsensical summary of an aggregate of plans.[28]

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Whatever it is, then, Soviet "central planning" is certainly not central planning. It is natural to enquire next how the "plans" are composed. This may afford us some clue as to what is really going on. Roberts has drawn attention to the curious fact that discussions of Soviet "planning" do not attempt to explain the *derivation* of the "plans." The origin and composition of "plans" are simply taken as given.

The "planning" system is a pyramid. At the top is a "plan" couched in broad aggregates. As it passes downwards from level to level in the bureaucratic hierarchy, it is amplified and fleshed out. Finally it reaches the enterprises where it is translated into full detail. But it is only this full detail which gives the aggregates any significance. The explanation is that information is also moving *upwards* within the pyramid. A draft "plan" is amended by a process of consultation and negotiation between the levels. The resulting "plan" is based upon recommendations and pleadings by directors of profit-making enterprises. How about the draft plan? That was probably formed by adding a few percentage points on to the quantities produced in the previous plan period. The fundamental mechanism of Soviet "planning" is now laid bare: *the planners ask the enterprises what they intend to do, and then instruct them to do it.*[29]

This should not be taken to imply that the whole planning procedure makes no difference to industry. Communication is always imperfect, and the "planners" have no clear idea of what they are doing. The process causes delays and mistakes. By the time they get their own projections back as "instructions," the enterprises have changed their minds. Furthermore, the planners are obsessed with gross quantities; they therefore usually modify the fundamental mechanism: they ask the enterprises what they intend to do, then instruct them to do it, *plus x percent*. There is also an order of priorities which guides the planners in their attempts to harmonize the demands of the various levels. This is a ranking of production objectives (military always top, consumers always bottom), the effect of which parallels the efforts of ordinary interventionist governments to mold industry by means of discriminatory taxes and subsidies.

It is usual for "plans" to be finalized after the start of the period they are supposed to cover, and they are then constantly amended in the process of "implementation." As Roberts dryly observes:

> The plan is changed so often that it is not congruous to say that it controls the development of the economy. There is an alternative possibility that the development of events controls the plan.[30]

Normally there is a five-year plan, divided into annual plans, further subdivided into quarterly and monthly plans. Pejovich reveals that

> the 1961 plan for the Tartar Autonomous Republic was modified five hundred times. When these modifications occur, in effect, the plan is constantly revised and brought in line with the business firms' actual

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> performance. Thus, in the course of the year, the plan and the economy's actual performance eventually converge and at the end of each year, the Soviet press can therefore honestly report that the annual plan has been fulfilled.
>
> For example, the average rate of growth of total industrial output was set at about 8 percent per year in the 1971–75 plan. The actual rate of growth in 1971 and 1972 fell to 6.1 and 5.4 respectively. Then, the Soviet government simply reduced the planned rate of growth to 5.8 percent per year.[31]

So, in addition to the plan's origin as, essentially, a summary of the plans of numerous profit-seeking enterprises, even that is ceaselessly revised in the light of unpredictable changes. This is as we would expect, for no one can know what the development of industry will encounter for the next five weeks, let alone five years. Industrial production is always a voyage into the unknown.

Some writers on the Russian economy, who do not challenge the hypothesis that it is planned, begin by summarizing the formal planning system, then comment that such a system seems unable to function, and next try to explain how it nonetheless can function, by giving a list of Soviet practices which are all ways in which central planning is abandoned or limited.[32] But there must be an ordering process in Russian industry, which keeps it staggering along, however inefficiently. The existence of gaps in a bogus ordering process cannot be sufficient. Roberts also makes the simple but telling point that if there is central planning, "theory and practice must merge."[33] If there is a planning method, the planners ought to be able to say what it is. But there is no theory to account for the derivation of Soviet plans, except the Polanyi-Roberts theory that they are aggregates of the separate plans of millions of autonomous profit-seeking enterprises.

Sovietologists who start from the premise that Russia is centrally planned display the naivety of an anthropologist who, upon being informed of the tribe's own theories of the world and their place in it, accepts them as true, and bases his fieldwork on them. Analysis of the Russian economy must start from the realization that there is no such thing as central planning. The sources of rational allocation are: (a) taking prices from the West; (b) copying technical processes from the West, thus taking advantage of the market-selected combinations of factors, and enabling costs of production to be roughly gauged; (c) taking prices and technology from Eastern Europe, where state intervention is generally much laxer than in Russia; (d) the legal and officially recognized internal market; (e) the internal market camouflaged as central planning; (f) the illegal (but none the less enormous) "black" market. The relative importance of these is a matter for empirical investigation, though Mises' view that only the first two are operative must be false.

Absolutely dependent upon the autonomy of profit-directed enterprises, the Russian system is still held back by the fact that enterprise directors are

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state appointees, and property rights in enterprises are not freely transferable. The initiation and closing-down of state enterprises is thus not determined on the open market. Property speculation, capital and money markets are non-existent or extremely rudimentary, but these institutions, thrown up spontaneously in a free society, play a vital role in coordinating modern industry, and there is no hope of Russia's approaching Western standards of prosperity without them. It will be interesting to see by what formulas they will be reconciled with Marxism-Leninism, unless the Communist Party is overthrown first.

NOTES

1. V. I. Lenin, *Collected Works* (Moscow: Progress; London: Lawrence and Wishart, 1960–), 32:364.
2. *Ibid.*, 33:65.
3. *Ibid.*, 33:113.
4. Referring to "the utopian hopes of the epoch of war communism," Trotsky concluded that even if the revolutions in the West had occurred "it would still have been necessary to renounce the direct state distribution of products in favor of the methods of commerce." Quoted in Paul Craig Roberts, *Alienation and the Soviet Economy* (Albuquerque, N.M.: University of New Mexico Press, 1971), p. 42, n. 27.
5. Lenin, *Collected Works*, 27:449.
6. *Ibid.*, 30:110.
7. Boris Brutzkus, *Economic Planning in Soviet Russia* (London: George Routledge and Sons, 1935), p. 106.
8. *Ibid.*, p. 107.
9. Alec Nove, *Economic History of the U.S.S.R.* (Harmondsworth, Middlesex: Allen Lane, 1969), p. 120.
10. Ernest Mandel, *Marxist Economic Theory* (London: Merlin, 1968; New York: Monthly Review Press, 1970), p. 553.
11. Nove, *Economic History*, p. 141.
12. Brutzkus, *Economic Planning*, p. 153.
13. *Ibid.*, p. 163.
14. Karl Marx, *Capital: A Critical Analysis of Capitalist Production* (Moscow: Progress; London: Lawrence and Wishart, 1974), vol. 1, chap. 21, p. 521.
15. Ernesto Guevara, *Che: Selected Works of Ernesto Guevara*, ed. R. E. Bonachea and Nelson P. Valdes, (Cambridge, Mass.: M.I.T. Press, 1969), pp. 112–36.
16. *Ibid.*, pp. 116–17.
17. *Ibid.*, pp. 118–33.
18. This is sometimes disputed in the case of Fidel Castro. He now maintains that he was always a Marxist-Leninist but had to keep quiet about it in order to gain power. Although his saying this now does not prove it to be true, it is fully consistent with all the evidence, and any other interpretation must make bizarre assumptions. Llerena argues that Fidel was not truly a Marxist-Leninist, but in order to read this aright we must realize that Llerena believes Castro is not a Marxist-Leninist now! Llerena's judgment is psychiatric. He views Castro as a psychopath convinced of nothing but his own importance. Llerena accepts that all Fidel's close associates in 1958 were Marxist-Leninists and that he presented himself to them as such. See Mario Llerena, *The Unsuspected Revolution: The Birth and Rise of Castroism* (Ithaca, N.Y.: Cornell University Press, 1978), pp. 198–204.
19. See Carmelo Mesa-Lago, *Cuba in the 1970's* (Albuquerque, N.M.: University of New Mexico Press, 1978). See also Edward Boorstein, *Economic Transformation of Cuba* (New York: Monthly Review Press, 1968). Boorstein, a Marxist economist who worked in Cuba, confirms the prior Marxist convictions of the rulers (pp. 18–19), shows how early

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they were set on a socialist course (p. 151) and predicts: "by the end of this decade, the full benefits of socialism will begin to show themselves in Cuba" (p. 225).

20. Charles Bettelheim, *Economic Calculation and Forms of Property* (London: Routledge and Kegan Paul, 1976), p. 120.
21. On the magnitude of Castro's failure, see for example Frederick B. Pike, *Spanish America, 1900–1970* (London: Thames and Hudson, 1973), pp. 151–57. For a detailed study, see Sergio Roca, *Cuban Economic Policy and Ideology: The Ten Million Ton Sugar Harvest* (Beverly Hills, Calif.: Sage, 1976).
22. I do not count the events in China under Mao or in Cambodia under Pol Pot. In China there was much emphasis on non-pecuniary incentives and other measures preparatory to communism, but there does not seem to have been the implementation of centralized allocation *in natura*. It appears that whilst the Cambodians did largely implement the abolition of money, they also fully intended the abolition of modern industry and a reversion to primitive conditions.
23. Mises, *Human Action: A Treatise on Economics* (Chicago: Henry Regnery, 1963), pp. 702–703.
24. Anthony C. Sutton, *Western Technology and Soviet Economic Development*, 3 vols. (Stanford, Calif.: Hoover Institution, 1968, 1971, 1973).
25. Maurice Dobb, *Socialist Planning: Some Problems* (London: Lawrence and Wishart, 1970), p. 27–56.
26. Abram Bergson, "Socialist Economics," in Howard S. Ellis, ed., *A Survey of Contemporary Economics* (Philadelphia: Blakiston, 1949), p. 447.
27. "Growth" means increase of national income (product). The national income is the total monetary value of goods (including services) produced (or what amounts to roughly the same thing, sold). The monetary value of capital derives from the expected future monetary value of final goods produced by that capital. If these final goods do not materialize, it means that the earlier national income statistics, which included production of capital, are to that extent misleading. If we observe "high growth rates" which take the form of artificially stimulated production of "capital," and subsequently there is no corresponding expansion of production of consumers' goods, we must interpret the earlier "high growth rates" as a statistical mirage. They did not really represent additions to capital, but something akin to firework displays, a waste except for the gratification afforded the Party members who contemplate the statistics.
28. Michael Polanyi, *The Logic of Liberty: Reflections and Rejoinders* (London: Routledge and Kegan Paul, 1951), p. 134.
29. This is the Polanyi theory which Roberts has advanced repeatedly in scholarly journals and in his *Alienation and the Soviet Economy*. For Polanyi's early statement of his view that there is no central planning in Soviet Russia, see his *Contempt of Freedom* (London: Watts, 1940), especially pp. 27–95. I do not know of any serious attempt to refute the Polanyi-Roberts analysis, though it has been corroborated by persons intimately acquainted with Soviet-style planning operations, who have declared "central planning" a complete sham. For instance, see Jerzy Gambit, "The Polish Economy: Models and Muddles," *Survey* (Summer 1971).
30. Roberts, *Alienation and the Soviet Economy*, p. 78.
31. Svetozar Pejovich, "The End of Planning: The Soviet Union and East European Experiences," in A. L. Chickering, ed., *The Politics of Planning* (San Francisco: Institute for Contemporary Studies, 1976), p. 101.
32. Under the heading "Ameliorative aspects of the planning process," Bryson explains that not all commodities are included in the central balancing process, the balances are not very detailed, some balances are assigned to lower levels, etc. See P. J. Bryson, *Scarcity and Control in Socialism* (London: Heath, 1976), pp. 8–9.
33. Roberts, *Alienation and the Soviet Economy*, p. 73.

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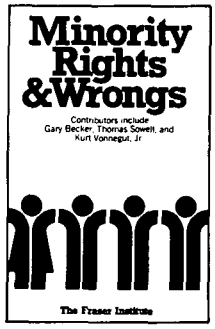

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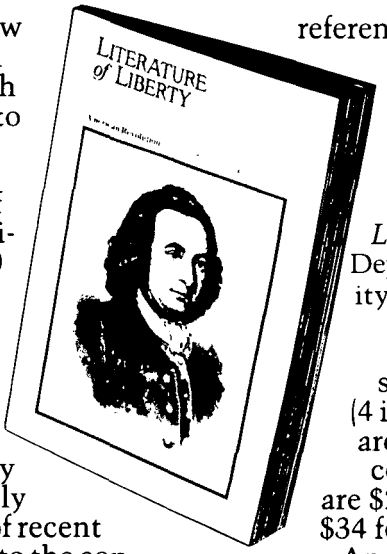

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